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Interpretation of the Russian Accounting Information

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Abstract

This thesis describes a simple technique of consolidation and reporting of Russian financial information for international users of accounting information. This thesis is also concerned with the recent changes in Russian accounting. The nature of the topic necessitates examination of a legislative change (i.e. the ongoing accounting reform) and an economic change (i.e. Russian financial crisis) as factors influencing Russian accounting. Inflation accounting and financial crisis are covered due to their significant influence on the requirements for the financial information. Furthermore, the unique recording methods of certain transactions necessitate a further examination of the accounting system down to bookkeeping entry level.

Keywords: Russian accounting, Balance sheet, Income statement, Inflation, Currency rate, Currency crisis, Performance measurement, New chart of accounts.

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1 INTRODUCTION

After the collapse of the former Soviet Union¹, Russia faced a great challenge to implement a market economy model to replace the socialistic system. One of the most distinctive characteristics in this development was a violent pursuit of free trade and free market economy. When the time of socialistic government was over, Russia became an attractive target region for many foreign importers.

Protecting its own struggling production Russian government implemented many barriers to foreign products in terms of tolls and taxes. In answer to this development, western companies opened affiliates, representative offices and joint ventures in Russia. The main purposes of these entities are to utilise their competence, to capitalize on the cost-effective local resources and to compete in local markets. Operating in Russian markets requires knowledge of the local legislation, regulations and general business conduct. Most of the difficulties encountered are of an administrative nature, but in the longer run, there might be many other things to be considered, e.g. organised crime, acquiring the right human resources, avoiding undesirable business relations, etc. When the unit has been fully established the administrative difficulties are usually of a financial nature, relating to accounting and especially taxation. Studying accounting and taxation will help to overcome most of those administrative difficulties in the long run, whereas most of the informal difficulties have to be processed when they emerge.

Goal of this thesis is to describe a simple technique of consolidation and reporting of Russian financial information for international users of accounting information. In international accounting, country differences are addressed through harmonisation of the accounting systems, and therefore this thesis is also concerned with the recent changes in Russian accounting. The nature of this topic necessitates examination of a legislative change (i.e. the ongoing accounting reform) and an economic change (i.e. Russian financial crisis) as factors influencing Russian accounting. Furthermore, unique recording methods of certain transactions necessitate a further examination of the accounting system down to bookkeeping entry level.

¹ Commonwealth of Independent States (CIS) replaced Soviet Union on Dec 8. 1991. CIS is an alliance of 12 of the 15 former Republics of the Soviet Union (Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kirghizia, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan).

2 INTRODUCTION TO RUSSIAN ACCOUNTING

Russian accounting system is a heritage from the socialistic era of the Soviet Union. The ongoing accounting reform is approximately halfway through, and there exists numerous features from the old system that still govern the accounting practice. Purpose of this chapter is to introduce the reader to the current Russian accounting system, its position in the field of international accounting, and to demonstrate the historical implications, which the former Soviet accounting system imposes on the current Russian accounting system.

2.1 Russian accounting in a framework of international accounting

In a global comparison, one could expect to find the most similarities between Russian accounting and accounting in other former communist countries (i.e. East European countries). Based on the fact that two countries used to share the same political ideology (i.e. communism) it might seem logical to draw an analogy between the accounting systems in those two countries. However, the fall of Communism initiated a sequence of rapid and rather profound changes that led the development of these formerly communistic accounting systems in to their own separate paths. According to Richard (see Walton, P., Haller, A. & Raffournier, B. 1998, 320), *“Despite of coming from a same mould, they are now, ... very different”*. In order to give a global perspective to the Russian accounting it is more constructive to compare Russian accounting with accounting in traditionally capitalistic countries rather than to compare it with the former socialistic countries whose accounting practises differ from each other mainly due very recent events and partially coincidental (Walton et al. 1998, 320) influences. Therefore, we will proceed to compare the characteristics of Russian accounting with characteristics of countries that represent either Continental European accounting systems (e.g. France, Italy, or Germany) or Anglo-Saxon accounting systems (e.g. U.S. or U.K.).

When discussing the specific characteristics of Russian financial accounting one must not overlook the influence of taxation. Russia is a country that has faced harsh economic realities throughout the whole of its post soviet existence. The poor economic situation has made taxation one of the fundamental questions in the Russian economy. According to Walton (1998,

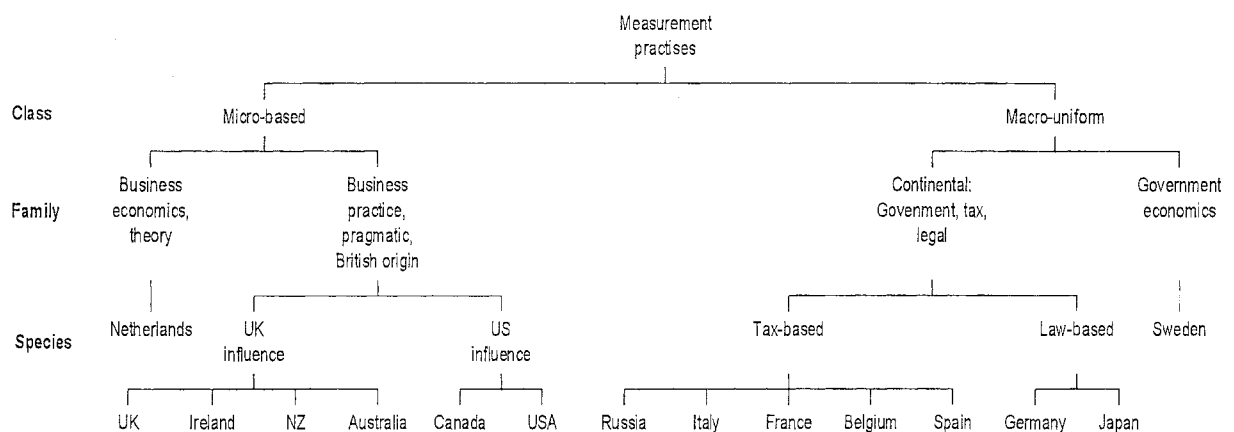
6), the influence of taxation on financial accounting arises in those countries where the financial accounting income is the direct base for the computation of income tax. In Russian taxation the base for the income tax computation is the profit or the loss of the year appearing in the balance sheet (for example, Walton 1998, 308). Therefore, Russia can be categorized belonging into those countries that have an accounting system that is strongly influenced by taxation and in this sense similar to e.g. Italy. According to Zambon (see Walton et al. 1998, 181), *“Italian accounting is regarded as law-based, tax-driven, ...and, as such, conservatively biased”*.

In terms of mechanisms of regulation (Walton et al. 1998, 6) as a variable explaining national differences of accounting practice, Russian accounting system is rather similar to Continental European accounting systems. For example, French accounting regulations are controlled by Ministry of the Economy, Finance and Industry, similar to Russian accounting regulations, which are controlled by the Russian Ministry of Finance. Further congruencies to the French accounting system can be found in the nature and the scope of the rules. Similarity of the nature of the rules is most lucidly conveyed in the likeness of the statutory chart of accounts that both of these accounting systems are build on, but also in the fact that both accounting systems include measurement and disclosure rules in their accounting standards. That is to say that the rules are rigorous in both countries. The scope of the rules relates to the nature of the rules and indicates how unanimously those rules apply. In Russia the existing disclosure rules apply to all companies, contrary to say, US, where the disclosure rules apply automatically to the limited liability companies (Walton et al. 1998, 7).

Further description of the Russian accounting system can be done via a classification of the legal system, which Nobes and Parker (1995, 12) categorize into two groups; one based on a common law and another based on a codified Roman law. Russian legal system is a typical system of codified Roman law, where the purpose of legislation is to establish detailed rules, and therefore the rules of financial accounting form the doctrine of financial accounting. Contrary to a codified Roman law, a common law is described as less abstract law that seeks to provide an answer to a specific case rather than formulate a general rule for the future (Nobes & Parker 1995, 12). In this categorization Russia belongs to the category of a codified Roman law countries, like for example, France, Italy and Germany, i.e. opposite to the common law countries like United Kingdom or United States.

Among those factors that shape the national accounting systems is also the role of providers of finance. The role of state in financing the corporate world determines the need for transparency in financial information; in those economies where capital is provided by the state or by banks, transparency is less sought-after than in those countries where finance is traditionally acquired from the public markets, because public companies must satisfy markets' information need in order to attract financiers. Russian companies have traditionally received their finance from the government either straight or through government owned banks, and the privatisation of the governmental companies did not increase the amount of shareholders appreciably, but shifted the ownership to "tycoons".

Figure 1 Russia among 14 other developed countries, hypothetical classification of measurement practices.



Based on the comparisons on the previous paragraphs, Figure 1² illustrates the position of Russian accounting system in a family tree classification presented by Walton et al. (1998, 23) *Tested hypothetical classification of measurement practices of listed companies in 14 developed countries* (see Nobes & Parker 1995, 71). The original classification is thus hypothetical, where the labels in the branching points are described as "short-hand" (Nobes & Parker 1995, 71) used to describe the attributes of the members of the accounting systems below them; actual outcome of this hierarchy is the grouping of the countries. Under this particular hierarchy Russia must be positioned to the group of tax-based accounting systems.

Finally, one of the most distinctive forces influencing the form of Russian financial account-

² Altered from Walton et al. (1998, 24, Figure 1.4) Tested hypothetical classification of measurement

ing must have been the financial crisis of fall 1998. A significant correlation between the financial crisis and legislative measures is impossible to state based on the promulgation dates of new accounting laws, because there is no information about the duration of the planning period, but a conclusion supporting a correlation between the financial crisis and legislative measures might be drawn from the fact that only one of the existing standards was promulgated before the financial crisis.

2.2 Main characteristics of Soviet accounting

Accounting system in the former Soviet Union was designed to meet the requirements of a centralized government and command economy (Keene 1997, 1). In the Soviet system the ministry in charge of the relevant branch of industry dictated the amount of enterprise's resources usage, production volume, and the prices of the finished products. Therefore, primary purpose of accounting was to provide information concerning production goals and consumption of resources (Matilainen 1997, 28). Campbell (1963, 13) describes the demands of accounting in the days of command economy as follows: *"In this situation it is necessary that the enterprise accounting be designed to produce information in the form needed by the central authorities. The concepts and categories used in the enterprise accounting must assimilate the planners' concepts and categories"* According to Makarov (1966) (see Walton, P... et al. 1998, 296) the superior nature (in terms of control) of the Soviet accounting system comes from a 'regulatory unity', which integrates accounting with operational and statistical data. The regulatory unity is achieved by complying with a principle of the 'unity of socialistic calculation'. In this socialistic calculation he recognizes three sorts of calculations:

1. Operational calculations, which are calculations of physical quantities, hence they are the governmental productivity calculations that measure whether planned production quotas have been met,
2. Accounting calculations, which represent financial statements (i.e. the balance sheet and the notes to the balance sheet), and
3. Statistical calculations, which represent the statistical balances that are required by the Governmental Comity of Statistics.

Administrative bodies gathered the result of the socialistic calculation using highly detailed reports, which the accountable filed four times in an accounting year. With the exception of the “Operational calculations”, the accounting- and statistical calculations have remained virtually unchanged throughout the accounting reform. They are still pre-printed standard forms, which Gorsky (2001, 1) describes as: *“derives from the ‘form over substance’ principle”*. Most significant documents of the annual accounts (forms number 1 - 6)³ are described in the Order No.4 “The forms of the annual accounts of an organisation”, last promulgated in January 4th 2000. The formal structure of the annual reports unquestionably decreases accountant’s latitude to consider substance over form principle while preparing annual accounts. Reason for this inflexibility concerning the annual reports is not solely in the accounting legislation, but also in the lack of reform in the public authority that issues these pre-printed forms. For example, the Governmental Comity of Statistics (GosKomStat) is the sole authority that can alter the form of the statistics reports⁴. As long as GosKomStat operates in the soviet style of bureaucracy, the statistics reports will remain mandatory, and they will most likely remain in their present fiscal form. It is noteworthy, that the statistics reports are designed for data gathering, and therefore the fiscal form can be justified by the data collection requirements.

Another distinctive feature of the socialistic system was that the state was the sole proprietor of the means of production. Therefore, the government was the only significant user of accounting information and the accountability relation existed only between the accountable and the state. Against this background, the fiscal requirements imposed on Russian accounting do not seem so overwhelming; they are merely a leftover from communistic version of user-oriented accounting. If one would imagine a nation as a single large entity, it would be rather logical for the government officials to prescribe a uniform chart of accounts to keep registration analogous, single depreciation method with fixed percentages, and pre-printed annual reports to ease the information collecting.

³ The balance sheet, income statement, explanatory notes of the income statement, cash flow statement, explanatory notes of the balance sheet, and the statement of capital usage.

⁴ For a further description, see appendix 2.

2.2.1 Role of profit in Soviet accounting system

Campbell (1963, 172) describes the role of profit in Soviet accounting as follows: *“In the Soviet system the primary motivation of the management at the level of the enterprise is to fulfil assigned plan rather than earn the greatest possible profit”*. Management’s lack of interest in seeking profit was totally rational because the planned production quotas were measured by productivity (hence output, measured in units) and the managerial performance was measured in ability to meet those production quotas. On the governmental level there was no attention brought to the profitability of the companies, because it was not important where the added value transferred into the nation’s economy. The general idea was that when a unit works in a closed system it has no influence to the system at large whether the unit is a cost efficient or not. That is, when the added value cannot cross the state borders it will be automatically allocated to the most cost effective unit. Campbell (1963, 13) defines the Soviet era accounting profit as follows: *“The Soviet enterprise has a profit, but the interpretation of this profit differs from what it would be in the capitalist balance sheet because of the different degree of autonomy which the enterprise has in disposing of it”*. This profit Walton (1998, 301) describes as *“revenue to the state’s capital”*, which rather well explains Campbell’s notion of the lack of autonomy in disposing the profit. Economising abundant resources (labour and energy) was therefore pointless, because companies had no real authority regarding the usage of earnings and because productivity was the key figure in performance evaluation.

It is also fair to say, that Russians have a history of undervaluing their depreciation percentages. In the Soviet Union time their depreciation costs, as a percentage of gross national product, was roughly 50% of the respective percentage in the U.S. The ratio between the percentages strongly suggests that Soviet depreciation charges fell considerably short on covering the cost of capital consumption. (Campbell 1963, 77). By undervaluing the depreciation percentages, the state was able to show higher return on capital, which denoted among other things higher GNP, therefore proving the Socialistic system more effective in respect to the capital system.

Russian accounting system is gradually adjusted to the requirements of the market economy. During the adjustment process this system is deemed to be a mixture of the

old and new system. A description by Gorsky (2001, 1) explains the current state of Russian accounting well: *“The current accounting system of the Russian Federation follows the Soviet path. It can hardly be any other way, considering that less than 10 years has passed since the break-up of the USSR. Businesses should be aware that there is no compatibility between Russian and any Western (U.S. GAAP, International Accounting Standards, or others) accounting systems”*. However, a reasonable level of compatibility can be achieved with a careful analysis of the accounting material⁵ and systematic reconstitution of the financial statements.

2.3 Accounting reform

Russian accounting reform is explicitly aimed towards harmonisation of the Russian accounting system with International Accounting Standards. After the accounting reform, Russian accounting is expected to respond better to the requirements of a market economy. Therefore the logical way improve the accounting system is by means of adopting the accounting practises of those countries that have proven success in acting as market economies. Most significantly, the accounting reform is expected to yield Russian Accounting Standards that should fully comply with the International Accounting Standards.

Soviet accounting practice rested on very different economic ideology than the economic ideology that exists in the modern day Russia. Therefore, the accounting reform is a colossal process that requires years to complete. The latest timetable for the accounting reform by Russian Ministry of Finance (hereinafter MinFin) expands the horizon of a complete adaptation of an *“IAS compatible accounting system”* until the year 2010 (ICAR May/June 2001, 1). The second ambition of MinFin is to install accounting profession as an active accounting regulator by the year 2010, which is a rather seminal reform in Russian accounting in the sense that it would transfer further development of accounting standards from MinFin to expert bodies.

The accounting reform itself can be considered a success, because the development has been both continuous and well focused. As an alternative for a gradual reform, an introduction of the entire new system at once would have caused an enormous change in the legislation. This

⁵ Primarily nominal ledger.

kind of legislative turmoil might have had rather catastrophic consequences. However, the deliberate accounting reform is viewed in a negative light mainly due to the bureaucratic obstacles that unnecessarily stall the process. The Technical Assistance to the Commonwealth of Independent States (TACIS⁶) describes the difficulties of the accounting reform as follows:

It is evident that the process of drafting and approving the new Russian standards and commentaries is going to be long (because of the revision cycles), complex (due to the overall complexity of the Russian bureaucratic structure) and contingent on the political environment changes concerning the Accounting Reform in Russia⁷.

Numerous revision cycles are needed to ensure that the highly detailed accounting standards are flawless, because those accounting standards are issued in a form of accounting acts. The necessity of the thoroughgoing legal codex can be explained with the Russian legal conception where “*something is legal unless explicitly prohibited by law*”⁸.

The accounting reform is a vast topic; one that alone would have enough substance for entire masters thesis. Therefore, this chapter might seem cursory, but the purpose is to demonstrate the connection between the accounting reform and the interpretations one should make from the Russian financial information. The harmonisation created by the accounting reform (i.e. by the time the reform is completed) should bring Russian accounting so close to IAS that the Russian financial statements would provide all the necessary information for consolidation and reporting purposes to those reporting under IAS.

2.3.1 International influence

The accounting reform explicitly sets out to adopt accounting practises of existing capitalistic countries thereby increasing harmony between Russian and international accounting standards. This process of harmonisation began right after the collapse of Soviet Union in numerous sectors of economy, including accounting. Russian accounting started to develop towards internationally recognized concepts like the True

⁶ TACIS is project funded by European union, where KPMG and the UN Conference for Trade and Development (UNCTAD) provide knowledge and expertise for Russian authorities regarding the adaptation of the International Accounting Standards as a part of the accounting reform.

⁷ TACIS: Standards Development Process. <http://www.tacis-accounting.ru/shema2.htm> 3.11.2001.

⁸ Honkanen, M., Widomski, S., Matinpalo, I. & Hultin, T. 1997, 121.

and fair view concept⁹ through changes in the accounting law. The federal statute “Financial Statements of an Enterprise” dated 28th of November 1996 states the following:

Accounting (reports) should give a reliable and full presentation of the organisation’s capital and financial state and also about the financial results of its activities. Accounting is considered to be reliable when it is formulated and composed in compliance with the law and the normative acts, regulating accounting in the Russian Federation (MinFin order No 10, Point 3.3).

Although the law does not explicitly mention true and fair view concept, reliable and full presentation should be close enough to be interpreted as a concept with the same tenor. The earlier (March 20, 1992) edition of this same law does not mention reliable or full presentation, but states that the accounting reports must be based on the accounting registries.

Two international organisations, the TACIS mentioned above, and ICAR¹⁰ (International Center for Accounting Reform) are strongly involved in Russian accounting reform with a purpose to unify the new Russian accounting standards with the International Accounting Standards.

TACIS is a programme with a purpose to provide general technical assistance in the development of Russian accounting regulations. Their main objective is to introduce key IAS via development of new Russian accounting standards¹¹. Their official aim is to present 10 new standards, of which 2 are drafts and 5 are already revised at least once.

ICAR provides professional assistance to Russian official bodies engaged in the process of developing new accounting rules based on International Accounting Standards (IAS). ICAR also aspires to disseminate IAS accounting standards by offering Russian translations of the IAS standards and by holding seminars about the IAS standards. For those interested in Rus-

⁹ EU, Fourth directive, article 2.3 “The annual accounts should give a true and fair view of the companies assets, liabilities, financial position, and profit or loss”.

¹⁰ ICAR was established by the European Bank for Reconstruction and Development (EBRD), American Chamber of Commerce, the German Business Association, the Foreign Investment Advisory Council (FIAC) and the Institute of Professional Accountants (IPA).

¹¹ TACIS: Project objectives. <http://www.tacis-accounting.ru/info2.htm>. 3.11.2001.

sian accounting reform, TACIS and ICAR are excellent sources of Russian accounting related information, especially to those that prefer to have this information in English.

2.4 The purpose of accounting

The three main tasks of Russian accounting are (Koslova, Parashutin, Babzenko & Galanina 1997, 38):

1. Forming complete and reliable information of the organisation's activities and its financial standing, which is necessary to internal and external users of accounting information.
2. Securing the information needed by external and internal users to control the compliance with the laws of the Russian Federation limiting the financial activity, appropriateness of that financial activity, and movements of cash, property and liabilities.
3. Preventing the negative results as a result of the entity's activities, and to declare internal recourses safeguarding financial stability of the entity.

In the pursuit of those 3 tasks, the accounting should meet the following requirements¹²:

1. Chronological accurateness.
2. Punctuality.
3. Reliability (documentation, inventory, evaluation and calculation).
4. Completeness of information gathering.
5. Continuity, it should be a constant presentation of the financial process.
6. Comparability between indicators in plans (prognoses) and in accounting results.
7. Economy of the accounting.

¹² Lecture Notes: Accounting. p. 6.

2.4.1 Russian accounting legislation

The formal basis of accounting is strictly defined in the statutes of the accounting law¹³ and in the accounting acts (a.k.a. Russian Accounting Standards). Russian accounting standards are published in a form of accounting acts, which means that every new accounting standard augments the accounting legislation. The accounting reform also necessitates some changes in the existing accounting acts and therefore the legislation concerning accounting has been on a continuous state of change since the beginning of the accounting reform program in March 1998¹⁴.

2.4.2 Russian Accounting Standards

The accounting acts are confirmed by an order of the Russian Ministry of Finance (MinFin). The following list contains those 14 standards that are thus far (November 2001) legally valid. The notation on the list serves informational purposes; one truly needs all that information to find the right document. Abbreviation PBU stands for “Poloshenie Bukhgalterskomu Uchety”, which translates to an accounting act. For Example, PBU1/98 is the 1st accounting act of year 1998. However, the document containing the act is itemized with the MinFin order number (For Example, number 60H). This MinFin order number may correspond to a numerous orders; hence the number of the accounting act is needed to select the individual order. With these criteria one should be able to find a document, which contains the order in the beginning, followed by the accounting act.

- Accounting policy - PBU 1/98 approved by MinFin Order №60H dated 9.12.98. Revised in order №107 dated 30.11.99. Effective from 1 January 1999.
- Construction contracts - PBU 2/94 approved by MinFin Order №167 dated 20.12.94. Effective from 1 January 1999
- Foreign currency denominated Assets and Liabilities - PBU 3/95 approved by MinFin Order №50 dated 13.06.95, which came into effect on 1 July 1995

¹³ Federal Law No.129 November 21, 1996 “On Accounting”.

¹⁴ Decision of the government of the Russian federation no. 283 of March 6, 1998 ‘*On the approval of the programme for the reformation of accounting in accordance with the international standards of financial reporting*’

- Financial statements - PBU 4/99 approved by MinFin Order №43H dated 06.07.99 Effective for financial statements covering 2000 and after
- Inventory - PBU 5/9 approved by MinFin Order №25H dated 15.06.98 Effective from 1 January 1999
- Fixed assets accounting - PBU 6/01 approved by MinFin Order №26H, dated 30.03.2001. Effective for financial statements covering 2001 and after
- Post Balance Sheet Events - PBU 7/98 approved by MinFin Order №56H dated 25.11.98. Effective from 1 January 1999
- Contingencies - PBU 8/98 approved by MinFin Order №57H dated 25.11.98 Effective from 1 January 1999
- Income of an Enterprise - PBU 9/99 approved by MinFin Order №32H dated 6.05.99. Effective from 1 January 2000.
- Expenses of an Enterprise - PBU 10/99 approved by MinFin Order, №33H dated 6.05.99. Effective from 1 January 2000
- Affiliated Party Information - PBU 11/2000 approved by MinFin Order, №5H dated 13.01.2000. Effective for financial statements of the year 2000
- Segment Information - PBU 12/2000 approved by MinFin Order, №11H dated 27.01.2000. Effective for financial statements of the year 2000.
- Accounting for Government Assistance - PBU 13/2000 approved by MinFin Order, №92H dated 16.10.2000. Effective from 1 January 2000.
- Accounting for intangible Assets - PBU 14/2000 approved by MinFin Order, №91H, dated 16.10.2000. Effective from 1 January 2001.

The second standard (PBU 2/94) is effective at the moment but according to ICAR: “it should be updated in accordance with the Russian Accounting Reform Program towards IAS¹⁵,”

At the moment (September 2001) under revision are the following drafts¹⁶:

- Standard on Income
- Equity Standard
- Standard on Cash Flow
- Standard on Depreciation of Assets

¹⁵ ICAR: <http://www.icar.ru/eng/page6.html>. 18.08.2000.

- Standard on Impairment of Assets
- Standard on Exchange Rate Differences
- Standard on Accounting for the Effect of Changing Prices
- Standard on Inflation Accounting
- Standard on Interim Reporting
- Standard on Contingencies

The existing standards are predominantly concerned with reporting and information presentation technicalities, while the drafts that are under revision are more concerned with inflation, quantifications, and cash flows. Most of these becoming standards, like the Standard on Income, are dealing with areas that are covered by the law on taxation, and therefore have a low priority. Standards like the Standard on Depreciation of Assets are directly connected to calculation of taxable income and not only inconsequential without respective changes in the tax legislation but also under scrutiny due the implications that these standards have on collected taxes. Standards on inflation accounting and accounting for the effects of changing prices have a common dilemma concerning the information deficiency caused by lack of reliable inflation indices. The IAS standard No 29 “Financial Reporting in Hyperinflationary Economies” provides the usage Consumer Price Index (CPI) as an indicator of the rate of inflation. In the Russian case, usage of CPI as an indicator of inflation rate is not a feasible option, namely because a reliable CPI is not available from the governmental organs, and therefore introduction of a standard on inflation accounting based on the IAS 29 may wait for a reliable measurement method of inflation rate.

¹⁶ TACIS: <http://www.tacis-accounting.ru/standards.htm>. 20.08.2001

2.4.3 Russian Accounting Law

Besides the existing accounting standards, financial accounting is regulated by the following documents that structure the accounting legislation, that is to say, apart from the standards:

1. The Federal Law “On Accounting”¹⁷ is the actual accounting law that defines the principal concepts of accounting, such as the function of accounting, accounting documentation, the responsibilities of the head accountant, content of annual accounts, etc. These concepts are defined in general level, to be then defined in detail in the accounting acts (Article 5 clause 2.b).
2. The new chart of accounts (Confirmed on 31 October 2000, effective from 1st of January 2001) (Kamyzanov P.I., A.P., & L.I. 2000, 393).
3. Notes on accounting in Russian market economy¹⁸. This document describes the requirements that a transition to the market economy sets to the accounting. Therefore, it describes the “new” interests groups and their information needs. This document is not compulsory in a way that it doesn’t take priority over any of the accounting laws or acts¹⁹.

2.4.4 Annual and periodical accounts

In Russian accounting the periodical accounts are reported four times in a year, each denoting an end of an accounting period. Each of these quarterly reports has the form of a Russian balance sheet and therefore they are called a quarterly balance(s). The fourth quarterly balance ends the accounting year; hence it is the annual balance. Small companies have to also submit one statistical balance every quartile. Large companies submit a statistical balance every month.

The balance sheet and all the supplements included into the balance have to be submitted to the governmental tax administration using the pre-printed official forms of

¹⁷ No.129-Fz of November 21, 1996, (Revised on July 23, 1998)

¹⁸ The presidential committee of Institute of professional accountants. 29 December 1997

¹⁹ Notes on accounting in Russian market economy: Article 2 clause 3.

corresponding governmental organ, for example, MinFin on the balance sheet, income statement and the notes to the balance sheet (the supplements to the balance sheet and income statement and explanatory notes are hereinafter referred to as the notes to the balance sheet).

The general directive concerning annual accounts is based on following documents:

1. Directive on annual accounts: "*Financial Statements of an Enterprise*" (Minfin order 43n), the second paragraph defines annual accounts as follows:

The financial statements include a balance sheet, income statement, their notes as well as the auditor's opinion that confirms reliability of financial statements of an enterprise subject to compulsory audits under federal laws²⁰.

2. Annual accounts forms and directions of filling in these forms are defined in standard "*Of Annual Reporting Of An Organisation*" (Minfin 1996, order No 97), which states the following:

The head accountant and the manager of the company must approve every annual, and periodical account with their signatures, and these periodical accounts must be delivered to the tax administration office personally, excluding statistical reports, which are issued to the Comity of Statistics. Large companies and companies with foreign capital deliver their reports to the central office, small companies without foreign capital use local offices.

3. The publication of annual account information in a stock company: paragraph 1.2 of the law "*About The Publication Of The Annual Reports In A Listed Company*" states:

The annual report is considered published in mass media, accessible for all the stockholders of the company, if the publication has appeared even in one printed periodical. This periodical can be defined in company's regulations, or can be chosen in a stockholders meeting. (MinFin 1996, No 101)

²⁰ ICAR translation at: http://www.icar.ru/eng/page6_4.html.

4. Instructions of the consolidation of the annual accounts on concern companies is defined in the law “*Of Methodological Recommendations Of Forming And Presenting Consolidated Accounts*”:

The consolidation has to be made if the parent has a control over 50% of the voting stock of the subsidiary company, or in limited partnership owns no less than 50% of the first stock. Consolidation has to be made also if the parent company can influence subsidiary's decisions by contracts made between companies, or in some other way can influence subsidiary decision making. The parent company has to include the information about the subsidiary company in its annual accounts if it has a control over 20% of the daughter's voting stock, or over 20% of the first stock of a limited partnership (MinFin 1996, No 112, point 1.3.).

Russian accounting model is a so-called static balance sheet model, where the primary objective of the financial reporting is to portray the economic situation of the company. Income computation is regarded merely as one stage of preparing the balance sheet. When the accounts are prepared correctly, the profit on the income statement equals the balance on the profit and loss account. The profit and loss account summarises the revenues and expenses and shows the profit or loss for the period as a difference after deduction of depreciation and provisions. Whether the accounting model is the main source of differences in the accounting systems could be discussed in great detail to produce an entire chapter of additional argumentation.

When the accounts are closed the auditor inspects the disclosure, and then the true purpose of the accounting is to verify the accuracy and rightfulness of the data given in the reports. Also tax inspections are usual, which typically means that the accountants prepare the accounts as if the tax inspection would be a certainty.

To categorise the general approach to an accounting theory, the vast majority of the Russian accounting professionals seem to favour the Tax approach to accounting theory. The Tax approach is defined in Accounting theory (Hendriksen, E., Van Breda, M. 1991, 4.) as: “*The approach favoured by many newcomers to accounting is to ask what the Internal Revenue Service (IRS) has to say on the subject*” It is note-

worthy however, that the tax-approach is also law-driven, since the taxation regulations have stronger legal force than the accounting law or the new accounting acts (ICAR, Dec 1999, 1). The accountants primary concern is to minimize the tax burden of the entity within the limits of the tax legislation. The accounting legislation is seen more as the guidelines to the technicalities of the accounting procedures and representation of the data.

2.5 Statutory chart of accounts.

The chart of the accounts in Russian accounting has a legal form. Statutory chart of accounts itemizes the main accounting accounts (also known as the accounts of the first order). The chief accountant may freely set up and utilize any desired sub accounts (the accounts of the second order) as long as they are related to the company's activities. Selection of sub accounts should target completeness and accuracy of the accounting (Koslova et al. 1997, 29). An account of the first order can be added to the chart of accounts only with a prior approval of the Ministry of Finance (Kamyzanov et al. 2000, 22)

The method of denoting the accounts has a numbering system, where a main account has a 2 digit number, followed by a one or two digit number denoting the sub account, divided using a dot (.).

A new chart of accounts was introduced in October 2000 and it has been valid since January 1st 2001. The changes brought by the transition to new chart of accounts are explained in the context account categories. Previous chart of accounts contained 9 main categories while the new chart of accounts contains 8 categories.

The basic form of the chart of the accounts has the following structure²¹:

1. *Fixed capital and other long-term investments* (accounts from 01 to 08). They include tangible assets, such as buildings, machinery, equipment, transportation equipment etc. and their depreciations. They also include intangible assets, their amortisation, increases in capital, and tangible assets under instal-

²¹ See appendix No 5 for the new chart of the accounts.

lation. A peculiarity is the attention to the life stock, apparently for collective farming purposes. The account 6 (long term financial assets) of the old chart of account will be terminated when converting to the new chart of accounts. The balance from the account 6 will be entered to the account 58 (financial assets) (Sizov 2001, 81).

2. *Current assets* (accounts 10 - 19). Includes raw materials, supplies and VAT items (account 19). In the old chart of accounts existed a concept of MBP item, which is an item of small price, and/or short time of usage. MBP is an abbreviation for Russian words of “cheap and fast consumable”. An MBP item can be written off 50 % at the moment of deployment and 50 % when it has been used completely. When converting to the new chart of accounts the value of those MBP items will be transferred to the account 10, sub account 9 (i.e. 10.9), because the accounts for the MBP items cease to exist.
3. *Production expenses* (accounts 20 - 39). Includes those expense accounts that are included into the production value. Accounts for components completed (account 21) and account for recognition of partially completed projects (account 36 in the old chart of accounts, 46 in the new chart) indicates the status of the production batch, which is vital for calculating production values for batches. Release of completed production is an account that is used to indicate product movement to the stock.
4. *Finished products, goods and sales* (accounts 40-49). Including expense accounts, which are included into the production value. Here the accounts are primarily due to a selling of the finished products and whether they can be accounted to be a part of the production value has to be decided according to the rules of calculating the production value²². With a new chart of accounts, 4 accounts from this group will cease to exist and one new account will be created. The account 44 will get a new name, “Sales expenses”, and it will consist of accounts 43 and 44 of the old chart of accounts. Account 46 will be changed to 90 “Sales”; hence it will be transferred to the 8th group. Account 36 from the previous group will then occupy the place of 46 in the new chart. The two other realization accounts (47 and 48) will be also moved to the 8th group under the account 91 “Other income and expense”(Sizov 2001, 130-135).

²² For a detailed description of the calculation of the production value, see paragraph 2.9.

5. *Monetary reserves* (accounts 50 - 59). This group includes cash money (roubles and foreign currencies) and money in bank accounts or in other financial institutions. Usually a company needs minimum of three bank accounts, one for Russian currency, one for foreign currency and one for the exchange operations. The third account, which is needed for the exchange operations, is for the monetary items that are on the way from the rouble account to the currency account or vs. (account 57) which can be translated as "transactions en route". The account 57 is needed for accrual accounting purposes due the large volume of monetary flows between the currency account and rouble account and the lengthy duration of the currency transactions. In the 5th group the change into the new chart of accounts causes the account 56 "Monetary documents" to become a sub account 3 of the account 50, hence 50.3 "Monetary documents". Account 58 will have a change of name from Short-term financial assets to financial assets, and the sub account 2 will become the sub account 3 of the account 55.
6. *Payable/receivable accounts* (accounts 60 - 79) include trade payables and receivables, prepaid taxes, unpaid taxes and social security. In the new chart of accounts the account 76 "Accounts with creditors and debtors" will combine 5 accounts from the old chart. In addition to current/old 76, it will consist of accounts: 63(which will become sub account 1), 65 (which will become sub account2), 77, and 78. The account 61 will be closed to the account 60, and account 64 to account 62. The account 67 will melt into account 68.
7. *Capital and reserves*²³ (accounts 80 - 89); includes basic capital items, and Russian peculiarity, the funds for social expenses, consumption and cumulating of profit. In this group the change to the new chart of accounts will cause numerous changes: accounts 80 and 81 will be combined to account 99 that belongs to the next group. Also the account 82 will be terminated, and its sub account 1 will go to the account 63 and sub account 2 to the account 59. The account 89 will become account 96 of the next group.
8. *Financial result* (accounts 90 - 99) includes gains and loses, differences in rates, differences in amounts, and usage of gains (e.g. tax on gains). In this

²³ Previously 2 groups: Financial result (accounts 80- 84) and Capital & reserves (accounts 85 - 89).

the group the accounts 90 through 95 of the old chart of accounts will be terminated to accounts 66 “Short-term credit and loans” and 67 “Long-term credit and loans” depending on their maturity. Account 96 will become account 86.

There are some accounts in the Russian accounting chart that have a 3 digit numbering, and are called “Non balance sheet accounts”, or “Outside of the balance sheet accounts”. These accounts are used for recording of assets that are under company’s control but are not actual property of the company. They include e.g. rented production equipment, valuables taken for safekeeping, products in rework (warranty), items of commission trade, equipment awaiting mounting, etc. Entries to these accounts are entered as a single entry. Change to the group of “non-balance sheet accounts” due the new chart of accounts will deliver on new account 010 “Depreciation of basic capital”, which will combine old accounts 014 and 015. Furthermore account number 021 will be numbered as 011.

Accounts are also divided into syntactic and analytic accounts. Analytic accounts are accounts to which are usually used for accounting entries. Syntactic accounts are the accounts used to compile closing balances from the analytical accounts. Main accounts are very often syntactic accounts. A sub account can be either syntactic or analytic. Syntactic accounts are seldom used to record accounting entries apart from certain financial transactions that are recorded directly to the profit/loss account.

For example the account No 02, “Depreciation of Property” can have the following sub accounts:

02.1 “Depreciation of Property”

02.2 “Depreciation of Long-term leased property”

02.3 “Depreciation of leased property”

2.6 Recording of the accounting entries

The recording of the accounting entries is done using causal double entry bookkeeping. There is as clear logic to the accounting entries as in any system of causal double entry bookkeeping. Therefore, we will concentrate on those recording rules that characterize the Russian accounting. Following examples are illustrated by T accounts in appendix number 1. For practical reasons, we will use the new chart of accounts for this example (example from Matilainen 1997, 42-43).

Purchase of material and a payment from the current account must be one of the very basic accounting entries (Entry 1). Material is recorded to the stock on accrual basis (Entry 2). At this point the VAT is separated from the price of the batch (Entry 3). Finally, the purchase price is recorded into an expense account when the material is deployed (Entry 4).

Entry 1	Per	60 "Accounts with suppliers"	an	51 "Bank account"
Entry 2	Per	10 "Materials"	an	60 "Accounts with suppliers"
Entry 3	Per	19.3 "VAT on materials"	an	60 "Accounts with suppliers"
Entry 4	Per	20 "Main production"	an	10 "Materials"

A more interesting operation is the recording of the accounting entries when a production batch has reached the end of a production cycle because then the value of a single product is determined the first time and the corresponding expenses are activated. For moving the finished products from the production process to current assets, it is possible to use or not to use cards to define the content of the production batch. These cards contain the information of raw materials and other components used to create the batch. This is a very Russian system, which can be avoided by using a Computerised accounting system. When using a computerised system, a list of the finished products and their movements between storage facilities has to be formed on a monthly basis.

In the second operation the finished production is first moved to the stock with its estimated production value. The realised production value is greater than the estimated production value. Therefore, at the end of the month a corrective entry is

made to adjust the difference to the sales account.

Entry 5	per	43 "Finished products"	an	40 "Release of production"
Entry 6	per	40 "Release of production"	an	20 "Basic production"
Entry 7	per	90/40 "Release of production"	an	40/90 "Realisation of products"

On entry 5 the batch is moved from account 40 to account 43, hence, from production to the stock, at the estimated production value. In case of retail type of business, account 43 is replaced by account 41 "Goods". If the batch is been sold straight outside of the company, the used account is 90 "Realisation of products".

On entry 6 we enter the actual production value. Account 20 belongs to the production expenses group, so here the actual production value causes expenditure to the company's books. So far the expenditure has been only in accounts that have no effect to the financial result. This method of expenditure recognition causes a timing difference, which has to be corrected, if one wishes to apply accrual accounting rules to Russian accounting entries.

On entry 7 the difference (that may also be negative) is entered to the sales account, because the product will go to the sales division with the estimated production value. After the operation the account 40 is closed.

To close up the simple cycle of one batch in the entity, one more operation should be made in which we record the sale of the batch. For a sale, 5 entries are required. First of those entries is to sell the product on credit, so that we have to record a sales receivable (entry 8). Then we have to record the VAT of the sold production (entry 9) and the production expenditure from account 43 to the sales account 90 (entry 10). When the customer has paid the sales receivable, the payment can be recorded to the receivables account (62) and the account can be closed (entry 11). The taxable profit resulting from this sale is the remaining balance on account 90, which is then recorded to the Gains and losses account No 99 (entry 12).

Entry 8	per	62 "Accounts with clients"	an	90 "Realisation of products"
Entry 9	per	90 "Realisation of products"	an	68.5 "Payments to the budget"
Entry 10	per	90 "Realisation of products"	an	43 "Finished production"
Entry 11	per	51 "Bank account"	an	62 "Accounts with clients"
Entry 12	per	90 "Realisation of products"	an	99 "Profit/loss"

A written presentation of the Russian bookkeeping system might seem complicated, albeit there is a very clear logic to the Russian bookkeeping system. The fact that the production value plays an extensive role in Russian accounting does not change the basic rules of accounting entries. Therefore, usage of accounting material as a data source results a straightforward and above all more precise method of corrective calculations than what is attainable on the basis of mere annual accounts.

2.7 Depreciation

In Russian accounting the depreciation is calculated monthly. Every month the accountant performs a depreciation of 1/12 of the yearly norm to the balance sheet value of the item (Bezrukih, P.S. 1996, 84). The percentages, which follow the norm, can be found from government resolution number 1072. For example, for a building there exists seven different depreciation percentages, ranging from 0.4 up to 10.0 per cent depending on the buildings construction materials, number of floors, purpose of usage, and so on. A typical depreciation percentage for a production facility would be 1.2 per cent. The bigger percentages are for buildings that are seldom used as a production facility, e.g. cottages made out of wood (5%). The smallest percentages are for apartment buildings (if the building has above 25 floors the percentage is 0.4%)²⁴. So, if we have a factory, which falls into the category of 1.2 % depreciation, it would takes us $(100/1.2)$ 84 years to convert the acquisition price into a cost. The depreciation must be calculated from the acquisition price of the item, which is in Russian accounting quoted as the balance sheet value of the item. It is noteworthy that the depreciation account 02 should have sub-accounts that are classified according the types of assets (Sizov, A.J. 2001, 16). The balances on these depreciation accounts are deducted from the balance sheet value of the assets in the closing of the accounts. However, the assets are carried for-

²⁴ The percentages are what Russian ministry of finance had confirmed for the year 1999.

ward with their original nominal value, as well as the cumulative amount of the depreciation, hence, the depreciation is kept apart from the asset.

Planned depreciation methods:

There is a concept of planned depreciation known in the Russian accounting system, but for taxation purposes it does not apply, and therefore it is seldom used. The planned depreciation is limited to the double depreciation²⁵. In other words, if the depreciation standard is 4 per cent the depreciation maximum is 8 per cent, but the effect of the additional 4 per cent has to be eliminated from the final result in the tax report. The elimination is applied simply by a corrective entry, after which the profit tax and the tax on assets can be quantified on the same basis, as would the standard depreciation result.

According to the government statute 6/97 (effective from January 1st 1998) (Kamyzanov et al. 2000, 507), other possible methods of planned depreciation are as follows (Matilainen, T. 1998, 4):

- Linear depreciation on the basis of the original acquisition price distributed through the time of economic usage.
- Declining depreciation, where the basis for the depreciation is the balance sheet value at the beginning of the accounting period.
- Straight-line depreciation on the basis of the original acquisition price.
- Substance depreciation, according to usage.

In all depreciation methods, the actual write-off must be performed for current month on the first day of the consecutive month at 1/12th of the yearly amount (Bezrukih, P.S.1996, 84). Among Russian accounting professionals the reluctance to use planned depreciation methods is due the extra work and the absence of any taxation advantage.

²⁵ Kovalev, V.V. & Patrov, V.V. 1998, 45 and Kamyzanov P.I., A.P. & L.I. 2000, 59.

2.8 Cost accounting

The most underdeveloped part of the Russian accounting system is, without doubt, their cost accounting system. The development of cost accounting has been left without attention during the long years of systematic planning of the nations economy. The cost accounting method used in Russia is a production value system. Concept of production value means the total value of expenses used in production, such as natural resources, raw materials, energy sources, assets, labour, and other expenses consumed in sales and production (Kamyzanov et al. 2000, 112). Those costs that are not in any way connected to the production process have to be recorded straight to the profit/loss account (Sizov, A.J. 2001, 148), such as, penalties of delayed payments, fines, and other sanctions. The exclusion of the overhead expenses is one of the reasons why the income statement usually presents a higher profit from the financial period than what it would be if made following western accounting standards (e.g. IAS). The income statement²⁶ is one supplement of the balance sheet.

The following list those items that are permitted into the production value by the Ministry of Finance (Matilainen. 1997, 48).

1. Direct production- and sales expenses.
2. Production supervising costs.
3. Product development and marketing (within certain limits).
4. Production process maintenance.
5. Customary costs of safeguarding and protecting employee's safety.
6. Administration of Production.
7. Overtime compensations, yearly- and other leave compensations, etc.
8. Payments made to governmental social-, pension and unemployment funds.
9. Mandatory expenses on employee healthcare.
10. Mandatory insurance.
11. Deprecations on non-financial assets.
12. Depreciation on intangible assets.

²⁶ Calculation of gains and losses (*Отчет о прибылях и убытках*).

2.9 Calculation of the production value

Production value is a cost per unit that is calculated from the total costs for each production batch separately when the product is finished. The finished products are transferred to the stock using account “Release of the production”, which is the number 37 in the old chart of accounts and the number 40 in the new chart of accounts. The counter account for Release of production is “Finished goods”, which is number 40 in the old chart of accounts and 43 in the new chart of accounts. This transaction is entered to the books with the average production value of the batch in question. This implies that the expenses in sales, advertising, freight etc. should increase the production value before calculating the taxable gains.

Quantification of production value is defined in the Russian Government statutes No 552 dated 05.08.1992 and No 661 dated 01.07.1995:

To the production value (labour, service) the enterprise includes expenditure, connected to the usage of surrounding resources in production process, raw material, material, fuel, energy, assets, labour resources and other costs of acquiring and realisation of these resources. (Koslova et al. 1997, 255).

For the actual valuation of the production batch value it is possible to use two alternative methods. Either the actual production value or estimated (normative, planned) production value. Actual production value is in practice very seldom used (sometimes in mass production), because it would require pricing of each batch separately, or the batches would have to be totally identical (Bezrukih, P.S.1996, 84).

As was said earlier, some expenses are regrouped into those that belong to the production value and those that don't. Administrative expenses, unless they result from the general administration, are not a part of the production value and they must be recorded to the gains and losses account. The consequence of this procedure is that the administrative expenses actually increase the written value of the enterprise instead of decreasing the taxable income. Payments due to breaking a contract or failing to fill all the terms e.g. court expenses, fines, penalties based on contract or any

sanctions of this nature are not included into the production value. Sanctions are recorded to account number 80 in the old chart of accounts, 99 in the new chart of accounts, and to the sub accounts accordingly (Baryznikov 1998, 409).

Some of the expenses decrease the amount of the unrestricted equity, and therefore are excluded from the production value. These expenses are considered to stay under enterprise control e.g. financing science, technology and innovation projects, technological work and costs of selling stocks, obligations, bonds or other financial instruments.

Whether an expense is a part of the product's production value must be determined case by case, unless it can be directly traced to the production batch or to one unit of the production (Kamyzanov et al. 2000, 118). All those non-direct costs that can be seen as a contributor to the production value must be somehow allocated to the corresponding batches. The costs are divided first into the analytic accounts on the recording phase, and then divided among basic production, service functions and management of services. For service functions and their management, the costs are counted separately by the content and usage of machine hours and equipment, division level management expenses (general production costs) and enterprise level management expenses (general management costs) (Kamyzanov et al. 2000, 118).

2.10 Calculation of the profit

When a product is sold, production value of the sold product is entered to the credit side of the account "Realisation of production", which is the account number 46 in the old chart of accounts and number 90 in the new chart of accounts. Income resulting from this transaction is entered to the debit side of the "Realisation of production". The profit of the single operation is therefore the balance on the realisation account, which is ultimately recorded to the Wins and losses account number 80. The realisation account is closed monthly, and the expenditure collected to this account is matched against sold production of the month. Exception is the transportation costs and the interest costs on loan capital, which are assigned to the entire production batch. Therefore, if there is unsold production at the end of the month, the remaining part receives a proportional part of these costs. As an example, the division of these costs

might be the following (Bezrukih 1996, 427.):

1. Transportation and interest expenses of the unsold production of the pervious month	900
2. This month's transportation and interest expenses	5100
3. This month's realised sales	308000
4. Leftover production in sales prices	90500
5. The amount of these expenses from this month's production $[100 \cdot (900 + 5100) / (308000 + 90500)] \%$	1.52
6. The amount of expenses being transferred to the following month $(1.52 \cdot 90500 / 100)$	1376
7. The portion of the expenditure of this month's production $(900 + 5100 - 1376)$	4624

All the other expenditure belonging to the production value is valued with its full cost. Taxable income (i.e. the basis for the profit tax) results when all expenditure belonging to the production value is deducted from the turnover, unless one chooses to issue dividends, which are profit tax reducible.

3 ADJUSTMENTS TO THE ANNUAL REPORTING

Compulsory accounting chart is one of the most troublesome diversities that thus far differentiate Russian accounting system from numerous other accounting systems. The fact that the Russian accounting chart is law-defined makes it rather impossible to design an accounting system that would comply both, Russian- and International Accounting Standards as such. According to Walton (1999, 11) in cases of a compulsory local accounting chart it may be necessary to keep duplicate accounting records. However, there is an alternative way to tackle reporting and consolidation difficulties, that of accounting locally using local prices and the converting the figures for consolidation (Walton 1999, 11). In the Russian case, a conversion process is deemed to be complicated because in addition to currency conversions, one has to consider inflation, and above all the differences in accounting practices between Russian accounting system and the targeted (by the conversion) accounting system. This chapter draws attention to those differences through an itemised examination of typical annual reports. These items are naturally a result of numerous accounting entries, and thus the autonomy of the accountant concerning the accounting entry techniques makes this technique further problematic. Therefore, usage of sub accounts in this chapter is limited to those cases where the sub accounts are explicitly mentioned in the law (i.e. there exist only one way to record a particular entry). Furthermore, the company can redefine parts of the accounting practice in its accounting policy.

Russian annual reports practically dictate the information requirements of the Russian accounting. These fiscal purposes require a completely different type of information than what would be needed for reporting to other interest groups, i.e. reporting that could be characterized as user-oriented reporting. Therefore, in addition to what was said earlier about the taxation etc. adjusting to the changed information requirements necessitates some recalculations based on the Russian accounting material. Those recalculations are contemplated in a context of separate items of the income statement and balance sheet. Next paragraphs discuss the main issues concerning those recording techniques that constituent the most distinctive differences of a certain item. When reading this chapter, it is advisable to utilise appendixes 4a – 4c, which introduce one model of income statement and balance sheet with a corresponding

Russian accounting account(s) for every particular item. It's also advisable to utilize the appendix number 5 that contains the chart of accounts.

3.1 Reappraisal of the financial statements

The reappraisal of some items of the annual reporting might necessitate historical data instead of mere recalculation based on the current financial statements or accounting material. The first correction to be considered is the profit/loss of the previous periods. If the adjustments to the annual report are carried out for a company that has done accounting only by Russian standards in the previous periods it is rather axiomatic that there is a substantial historical distortion in the profit/loss of the previous periods. Consequently the balance sheet value of the company is expected to be different from what it should be following the western standards, given that the valuation criteria of certain balance sheet items also contribute to these deviations. The above-mentioned balance sheet items are examined closer in the following paragraphs.

Depreciations play a key role in the asset valuations. The fiscal boundaries of depreciation and asset revaluation must be compared to their western counterparts to aggregate the total distortion of the balance sheet values.

3.1.1 Main considerations in the income statement

Recognition of expenses: The accrual basis for profit calculation requires that all the expenses should be recognised when they occur. For example, when in a Finnish accounting system a bill of a purchase is received, the expenditure is recorded in the accounting system. In the Russian accounting system this does not happen, but typically the expenses are recognised when the finished product is moved to the stock. When the production batch is transferred from the production to the stock it is valued on the production value basis, and at that point the expenditure is recorded as costs in the accounting system (Bezrukih 1996, 301). Material expenditure is generally recorded in the account 40.1 (retail) or 40.2 (wholesale) credit (Sizov 2001, 61), when the production is released from the plant. When the actual purchase has been realised, the entry is debit 41 "Goods" and credit 60 "Trade payables". Therefore, in order to make a proper recognition of the expenditure, one should take the balance from the debit side of the account 41, those entries where credit entries are at account 60.

Depreciations: Apart from the value of a particular balance sheet item, the expense caused by the depreciation naturally impacts the result of the financial period.

3.1.2 Main considerations in the balance sheet

Retained profits/accumulated loss, or the income of the previous periods should diverge from the actual profit figures if the earlier accounting profits have not been corrected. Computing a correct amount of retained profits using only the profit figures can be impossible without any further information of the prior periods. Therefore, the more preceding periods are performed using Russian accounting standards; more difficult it is to find the accurate figure. However, at the end of a period the profit can be found from the credit side of account 99 in the new chart of accounts and 80 in the old one. The balance results from matching the period's expenditure to these accounts, and therefore a debit balance naturally shows a loss (Kamyzanov et al. 2000, 176).

The retained profit or accumulated loss is recorded to account number 84 (counter account 99 is then closed) in the new chart of accounts (Sizov 2001, 123) and account number 88 (counter account 80 likewise closed) on the old chart of accounts (Bezrukih 1996, 441). Since all the retained earnings so far have been recorded using the old chart of accounts, we shall have a closer look at the account 88, which has the following sub accounts:

- Undistributed profit or loss of this period (Account 88.1). If there is a negative balance in this account, it should be distributed to the following 5 years, which means that the loss has to be deducted from the taxable profit in next 5 years.
- Undistributed profit or loss of the previous periods (Account 88.2) that contains those profits of the previous periods, which are not used for Accumulation, Social, or Consumption funds.
- Accumulation Fund (Account 88.3). This fund is usually used to prepare to finance some future investments, or for example, product development. It can be used to cover the losses of the accounting period, to cover the costs of financing on the accounting period or to distribute a part of the gains to the owners. This fund is quite seldom used outside industrial production.
- Social Fund (Account 88.4). Used for the entertainment and relaxation purposes of the

personnel of the company, for example, a trip to theatre. In general the social fund and the consumption funds are established to safeguard the well being of the company's personnel (Bezrukih 1996, 458).

- Consumption fund (Account 88.5) is a fund, which can be used to cover those costs that are not otherwise supposed to be paid within the rules of the accounting system. For example, an employee who has to travel on business is entitled to a daily allowance that is intended to cover the additional expenses caused by the travelling. Standard daily allowance is 22 roubles a day, but the company is willing to pay, say, 200 roubles. This difference of 178 roubles can be paid from consumption fund (Koslova et al. 1997, 392).

Funds are used because they lower the total tax burden of the entity: "*At the profit taxation, the assets transferred to the reserves are deducted from the gross profit of the company*" (Bezrukih 1996, 462). The funds are established simply by a debit entry to Usage of gains and a credit entry to the Retained earnings, sub account. With the new chart of accounts these special fund accounts have been removed while the equity accounts have become much more detailed²⁷.

Uncertain receivables: For uncertain receivables company has to establish a fund at the end of the accounting period. If all the methods of collection possible have been used without success, the organisation has a right to reserve the nominal value of the debt in a fund (Bezrukih 1996, 463). The reserved amount can be written off as a credit loss during the following accounting period. This means, that the uncertain receivable will be a balance sheet item in at least two periods (years) before becoming a credit loss. "All the methods possible" are understood, in practice, as filing a lawsuit and finding the debtor bankrupt. In the taxation however, both of the parties are liable for a profit tax if a liability is left uncollected. Creditor has already paid income tax, which will not be reimbursed regardless of the state of the liability i.e. whether it is collected or not. Debtor has to pay the tax when the liability has remained three years uncollected. After three years the debt is considered cancelled and therefore yields an income equivalent to the debt. In Finnish accounting legislation the credit losses have to be recorded when they become obvious, i.e. at the point in time when it is obvious that the credit cannot be collected. If the receivable is only partly lost then only this part should be written

²⁷ The new chart of accounts approved. ICAR newsletter. November/December 2000.

off and the rest should remain in the balance sheet (Järvinen, Prepula, Riistama, & Tuokko 1998, 378).

Revaluation of assets: This problem has become quite significant after the collapse of the Soviet Union, due to the very unstable value of the Russian currency (RUR). The balance sheet values of most of the balance sheet items have no correspondence with the current values of these items. As an example - a building bought autumn 1998. The original price of the item, RUR 1.200.000 would have been around USD 200.000. By the end of year 2000 RUR 1.200.000 would have been less than USD 50.000.

The company has the possibility for an elective revaluation every year, which also gives a possibility to revalue only a certain asset or a group of assets. Mandatory revaluation is all-inclusive (Bezrukih 1996, 94). Mandatory revaluation of assets is forced by a governmental order; hence, the government gives out an order for all the accountable to do a revaluation of their assets during a specific accounting period. The Governmental committee of statistics announces the index for the revaluation no later than 15th of the preceding year. Following the index for the year 1999, the revaluation coefficient for a production facility bought at the third quartile of 1996 would be from 1.06 to 1.21, depending on the location of the facility. The coefficient (index) is used to multiply the balance sheet value of the asset, and this results in the new balance sheet value. A mandatory revaluation was last ordered in the year 1998, whilst year 1999 onwards they have been voluntary.

Following a prudence principle, any revaluation that increases the value of the balance sheet should not enhance the financial result (Järvinen et al. 1998, 56), but the increased value should consist of only an increase in capital. In the Finnish accounting law, chapter 5, article 17: *A sum equal to the revaluation must be shown under capital in the revaluation reserve*²⁸. Furthermore, in Finnish accounting law, a building (construction etc.) cannot be the subject of a revaluation (Ernst & Young ltd. 1997, 9). Russian accounting system records the revaluation amount to the "Additional assets" or to the "Undistributed profit", sub account Social fund (Bezrukih 1996, 94). Therefore these entries have no effect on the financial result.

²⁸ The Finnish Institute of Authorised Public Accountants 1998.

3.2 Collecting figures from Russian accounting material

This method of collecting figures from Russian accounting material is also quite arbitrary in the corrective entry phase. On the other hand, it is a quite a simple system as long as the concepts are clear. Another point supporting this view is the lack of extra work required to produce the annual reports, if that is the sole requirement for additional accounting measures.

For Russian reporting purposes Russian accounting system produces a list of those accounts that have been used for bookkeeping during the accounting year. This list contains the turnover in each account during the period, the opening-, and closing balances, and therefore the list is similar to nominal ledger known in Continental European accounting systems. In Russian accounting, the nominal ledger is traditionally used to fill in pre-printed reporting forms. Using the nominal ledger it is possible to collect most the necessary figures to recreate an income statement or balance sheet of virtually any given reporting standard given that the differences in the accounting systems are addressed with due diligence. In a pursuit for better comparability it is recommendable that at least the corrections mentioned earlier should be made.

Also, should one want to be certain to obtain accurate figures, one should go through the entries rather than simply collecting the balances. For example, for the sales figure, crosscheck the entries between the realisation account (90) and the account number 62 "Sales receivables". The sums of the entries in the credit of account 90 with a counter account 62 results the correct amount of sales.

3.2.1 Items of the income statement

Income statement items require more attention to the accounting entries than balance sheet items, because income statement items are influenced more by a particular accounting plan than the balance sheet items. That is to say, that the a turnover in a closing account is totally dependent on the recording methods, as opposed to the balance sheet accounts, where the value of the item is dependent on the valuation principles.

3.2.1.1 Turnover

For accurate determination of turnover one needs the sales figure, which is the credit balance on the account number 90 (Kamyzanov et al. 2000, 111), because when a sale has been completed and product therefore has been shipped to the client, the bookkeeping entry made to the Russian accounting ledger is 62 debit and 90 credit with the transactions gross value (Kamyzanov et al. 2000, 129). Since account number 90 is a realization account, mere balance should be adequate for all practical purposes. However, since the Sales account is a syntactical account, it is possible to itemise following to specific sub accounts (Sizov 2001, 128):

- Turnover (sub account 90.1),
- Production value of sold production (sub account 90.2),
- VAT receivables from the clientele (sub account 90.3),
- Excise duties (sub account 90.4) and
- Customs duties (sub account 90.5)

There are multiple realization accounts in the old chart of accounts, ones that can be used to record a sale of fixed assets (47) or other non-current assets (48). However, the new chart of accounts will have only one realization account (i.e. number 90) Sales²⁹ and then the account balance needs to be analysed (to crosscheck the entries).

The account for the paid VAT is usually 68.2 unless the accountant has chosen to use another sub account of account 68. Usage of another sub account is perfectly possible, but rather unlikely to occur. Given that the account 68.2 is used for recording of VAT, its credit balance must be deducted from the credit balance on account 90 in order to arrive to VAT free turnover.

Furthermore, one should deduct the amount of sales tax 5% and the Road tax³⁰ 2.5% from the turnover, because the Sales tax and the Road tax are calculated on a gross sales basis; hence they are dependent on the sales volume. This way one may obtain a turnover, which is free from direct taxation. The sales tax is a fixed 5 % from sales revenue, so the practice is to add 5% margin straight to the sales price. Account for sales tax is 68, but the sub account may

²⁹ ICAR newsletter. November/December 2000. The new chart of accounts approved.

³⁰ The road tax, or the tax on the usage of the highway network, is a local tax in St. Petersburg.

vary in different companies. The Road tax is calculated from the same taxation basis as VAT, and it is recorded to account 67.1 in the old chart of accounts and 68 in the new chart of accounts (Sizov 2001, 97).

Other adjustments to the turnover, for example, sales freights, are similarly found from the sales account. If one would wish to separate items like sales freights from turnover, one has to analyse the content of sales account on the basis of the entries made to the sales account. Analysing the content of a particular account can prove to be a difficult task without any help from the accountant who has done the original entries. This crosschecking naturally requires the accounting journals (without them it is impossible) but because of the different practices of different accountants the journals alone might not be enough. The figures themselves are what the service provider has charged from the entity. In the Finnish accounting law chapter 4 article 1 defines the turnover as follows: According to the definition of turnover, from the sales revenue of main business activities, one has to deduct given discounts, VAT and other sales related taxes (Järvinen et al. 1998, 335). In this concept, which follows the EU article 4 point 28, sales freights are not deducted from sales revenue, but to be seen as other costs. Discounts are very rare in general, and the sales are usually recorded at their net value.

3.2.1.2 Other operative income

Other operative income that does not result from main business activities is recorded to the account number 99 “profit/loss”, which in the old chart of accounts was account number 80. In order to determine other operative income, one has to go through the entries on the profit/loss account. Account number 99 is always analytical, which means that it does not have any sub-accounts. The source of the entries has to be determined by their counter accounts. In the Russian income statement other operative income is shown on the line 170, and other operative expenditure on the line 180 (Kamyzanov et al. 2000, 575). Russian income statement and balance sheet are described in the appendix number 6 at the end of this thesis.

3.2.1.3 Differences in inventories

Differences in inventories are also straightforward operation. The difference in inventories is the difference between the opening and closing balances at the account 41.1 and/or 41.2. The

account 41.1 represents the value of the goods stored to a warehouse, and the account 41.2 used to represent the stocks in retail sales. Possible problems we face with inventories are the same evaluation problems as with all of the valuation items.

3.2.1.4 Purchases

For accrual accounting purposes one should eliminate the timing difference of the expense recognition by analysing the credit balance of account 60. The amount of sales is obtained by adding up all the credit entries on the account 41³¹ or 10 that have the account 60 as their counter account. Account 41 is for a resale type of business and account 10 is a warehouse account for manufacturing entity (Bezrukih 1996, 351). This way one can comply with the principle of accrual accounting when recording the purchases while receiving the goods. If one wishes to record an expense when one has bought the goods, one should take the entries, which are recorded debit 60, credit 51. The source depends in general of the method of cost recognition, but also of the accounting principles of the Russian accounting entity. This implies that if the entity is not really producing anything, there should be no problem. However, the problem arises, if we are producing something, which require in-house trade; without a proper mark-up the transfer price will settle too low considering the entity as whole, because the stocks of own production are usually valued at the production value.

If the division producing components is using production value system to price its production, a major part of the indirect costs will be excluded from the 'transfer price', following the previously explained taxation guidelines. Correcting this problem without any preconception of the costing method is a difficult task to do, and afterwards easily impossible, but still something, that has to be taken into consideration when evaluating the final productivity of a particular division.

3.2.1.5 Differences in rates

Differences in rates are a complicated matter because Russian accounting system entails two different but very similar concepts. A difference in rates typically result from open pay ables

³¹ If the sale has been recorded with the net value, then the account 19.3 should be added to the amount of purchases in order to include the VAT to the gross price.

or liabilities in foreign (non-Russian) currency (traditional sense). A very common practice in Russia is to value all the trading in USD. Therefore it is possible to get a currency rate difference while only Russian roubles are used for the transaction, in case the dollar value of the Russian rouble changes. In Russian terminology this rate difference is called “A difference in sums”.

In the current chart of accounts with the old law of income and expenditure differences in rates were entered to the account 80.4 “Rate differences”, or if the organisation don’t use this account, the differences in rates was recorded directly to the account number 80 (Kamyzanov et al. 2000, 143). With the new law³² the differences in rates is handled like previously, but since in the new chart of accounts account 99 replaces the account 80, this causes some consideration. Before the law change (effective from 1 January 2000) the difference in sums was regarded as a financial item, subject to the profit tax and VAT (Kamyzanov et al. 2000, 142), but in the old chart of accounts a *gross amount* was recorded to the account 80. With the new law³³ the difference in sums for simply a part of the monetary value of the transaction. The net difference is entered to the account number 46 and the VAT to the account number 68 (Kamyzanov et al. 2000, 144). Russian accounting tends to see the real rate difference, which results from the foreign trade, as a financial item, so that it would appear lower in the financial statement, but it still has a full effect on the taxable result.

3.2.1.6 Salaries

Amount of salaries paid is a credit balance on the account 70. Salary expenditure is registered by a credit entry to the salaries account and a debit entry to the expenditure account of the resource consumer, i.e. 20, 23, 25, etc (Bezrukih 1996, 167). Additional salary expenditure (i.e. holiday bonus etc.) can be debited from the account number 84 “Undistributed profit” in the new chart of accounts and account number 89 “Reserve for Future Liabilities and Charges” in the old chart of accounts (Bezrukih 1996, 167), but apparently the account 88.5 (Income of the previous periods) was more commonly used for this purpose in the old chart of accounts. For income statement purposes small adjustments are in order because the salary expenditure includes the employees income tax and the employees part of the pension payment.

³² Income of an Enterprise - PBU 9/99. and the Expenses of an Enterprise - PBU 10/99.

Because the tax withheld from the employee is a different with different employees, its possible to either deduct the balance on the account 68.1 from the salaries, or to omit the item of payroll tax from the income statement and to declare a gross salary expenditure. If there were salary advances paid, a credit balance opens the account at the beginning of the month. Or, as usually in Russia, the salaries are paid in the following month, so there should be a debit balance. This does not apply, because according to the law the salaries are paid twice a month, of which one is the advance, and the second is the remaining part of the monthly wage. Following the principle of accrual accounting, one should have an average of one month's salary expenses constantly as a payable in the balance sheet. Furthermore, if there are paid advances, the advance is all a salary expense, but to get the correct figure the deductions mentioned above should be made from the salaries in 70 credit. Combining these two figures results the right amount of salary expense for the period. Advances are all net salary expense, because the other expenses (including employee's income tax) have been posted to their proper accounts when the advances have been paid out.

3.2.1.7 Social costs

Salary related social costs are paid in similar fashion as the salaries, but they have to be paid prior to the actual salary payment. The salary related social costs are entered to the following accounts: Social security (Account 69 credit), Pension fund (69.2), Medical insurance (69.3 and 69.4, for local and federal budgets), and Unemployment fund (69.5). If these accounts have a balance at beginning of the period, they are related to the advance salaries paid, and should be included to the period's expenditure, as of course should the balance at the end of the period to be excluded, belonging to the next period.

3.2.1.8 Depreciation

Accounts for depreciation are accounts 02, 05 and their counter account is always 44. As was said earlier, in order to produce an alternative amount of a depreciation that would comply with some alternative standards, there's a need for a small corrective calculation. Provided that the balance sheet value of the item is correct, the corrective calculation for the depreciation can be conducted quite systematically. Otherwise one should try to determine the correct

³³ Minfin orders #32n and #33n. "Income of an organisation" and "Expenses of an organisation"

value of the item that is the object of the depreciation. One possible remedy would be to use the market price for the item, and then make depreciation for the item, according to an in-house depreciation plan. Another possibility could be to estimate the item's value to the company and use that as a basis for the depreciation. For consolidation purposes, one should naturally use the same evaluation and depreciation techniques as in the parent company. When doing a corrective depreciation, the purpose is foremost to correct the balance sheet value of the corresponding item but also to activate the proper expenditure. It's also recommendable that substantial corrections of the depreciation would be smoothened by distributing the corrective amount to more than one period.

3.2.1.9 Financial income and financial expenditure

Financial income and financial expenditure are recorded straight to the profit & loss account.³⁴ Financial income has a balance at the account 80/99³⁵ credit, and the expenditure has a balance at the account 80/99 debit. When determining the value of these items, account 80/99 has to be analysed, because the balance on this account is composed of entries that have no relation to the financial items. For example, interest income can be recorded to account 51 "current account", but there could be others, depending on the nature of the source of income. Income due the crediting the clientele has various counter accounts, e.g. D60, D76, D52 and D94 in the old chart of accounts. Other financial income should be determined naturally as the left over, which cannot be allocated to any of the other "classes".

Financial expenses use same accounts as financial income only in an inverse recording order. For Example, interest expenses quite logically have an inverse order compared to entries of interest income, which means that the interest expenses of the "current account" are those entries at account 80/99 debit, which have a counter account 51. Most significant item of financial expenses is the account for interest of delays and increases on taxes. It has a credit counterpart on account 68 "accounts of taxation". Another obvious group at the moment is the currency exchange expenses, which has the same counter accounts as the exchange income. The Russian practice on currency exchanges tends to be quite complicated, which makes them

³⁴ In some cases of financial expenditure the percentages of loans can be entered to accounts 20 and 26, if the payments actually decrease the loan capital. This way the percentages would be tax deductible, but the requirement of usage of analytical accounts is also mentioned, which implies that the expenditure will be cancelled in the taxation.

rather expensive.

3.2.1.10 Extraordinary income

Extraordinary income (when it results from a sale of fixed asset) has a balance on the debit side of the accounts 47 “Sales of founding assets” and 48 “Sales of other assets” or with the new chart of accounts, since there is only one realization account, it is 46. The counter accounts are 01 and 04. Problems regarding other extraordinary income and extraordinary expenses can be resolved with adequate sub account(s) that the accountant has a freedom to choose within the accounting policy of the entity. Furthermore, none of the extraordinary income or expense should result without prior approval of the chief accountant, because the chief accountant’s approval is needed for all transactions (Bezrukih 1996, 84).

3.2.1.11 Depreciation difference

Increase or decrease of depreciation difference is one of those items, which are totally dependent on the corrections made to the previous depreciations. If one should determine to use some other depreciation, than the Russian taxation law compliant yearly norm, it is advisable to have separate records for those items subject to the depreciation. It’s also recommended to have those separate books in some less fluctuating currency than Russian rouble.

3.2.1.12 Change in reserves

A change in the voluntary reserves is needed for a revaluation or annulment of the reserves. If there is a need to adjust the balance sheet items, which are formed from the financial result of some previous periods, the amount of reserves should be recalculated, because the basis for the reserves is in the distributable profit of the previous periods. The account number 89 “Reserve for Future Liabilities and Charges” is an exception, because it is quite seldom used, especially after the downfall of the Russian rouble at 1998. The account 89 is used to create funds for various needs e.g. repairing or renovating buildings, production facilities etc. The accounts for the funds will be omitted from the chart of accounts.

³⁵ The account number 99 will replace the account number 80 of the old chart of accounts.

3.2.1.13 Profit taxes

Profit taxes can be found from the account 81.1 (account 99 in the new chart of accounts) debit, with corresponding credit entries at the account 68 (Kamyzanov et al. 2000, 194). Other taxes are in the account 81 with counter account 68, but with a different sub account(s) than profit taxes. The sub accounts for the account 68 should be named by the nature of the payments. Actual quantification of the realized tax burden is by no means difficult. Only mistake the Russian accountants tend to do when composing IAS annual accounts, is to show the Road tax and the Sales tax among the indirect taxes, when they should be already reduced from the sales when calculating the turnover since they are assessed taxes.

3.2.2 Balance sheet items

3.2.2.1 Assets

The figures, which the Russian reporting system produces of non-current assets, are quite easy to find from the annual or periodical reports. The system of calculation of the balance sheet values does not considerably differ from, say, Continental European accounting systems. The items in Russian and western balance sheet correspond to each other quite well in terms of definition, but the evaluation through time causes a difference.

In current assets the correct value of inventories has to be determined, because it should be something else than the sum of production values of items in question. After this, forming the balance is a straightforward procedure.

3.2.2.1.1 Non-current assets

When intangible, and especially tangible assets are converted to comply some other reporting standard, they have to be usually valued by using some criteria. Balance sheet figures are easy to solve, because the assets are itemised in their own sub accounts. For a possible revaluation of assets against inflation, some methods are described in the next chapter. For example Accounts 01.01 "Buildings", 01.04 "Machines & equipment" 01.09 "Means of transportation (vehicles)" etc. are easy to identify to belong to a certain group in any style of balance sheet.

For the problem of revaluation there is no universal solution, because the value of an item (e.g. building) depends on the exchange rate at the acquisition date, items depreciation percentage, earlier revaluations, etc. All this was discussed in more detail earlier, and the wide variety of possible balance sheet value development chains makes further discussion futile.

Capital investments to monetary markets have their value determination done by the markets, so they must be accepted as they are. The possible changes on the value of these items should however be shown with their true value regardless the fact that they might not be recorded to the Russian accounting journals. Profit or loss on the capital investments (equity, bonds, etc.) is in Russian accounting practice recorded on a cash basis (Bezrukih. 1996, 104) (hence, when liquidated), which can lead to surprisingly constant balance sheet value over time. Since this item(s) has been traditionally considered as a valuation item, the value changes should be noted to comply with the accrual accounting principles. On the bonds however the difference between nominal- and the acquisition price is either depreciated or entered as income in equally distributed shares over the duration of the investment (Bezrukih. 1996, 311).

The division of capital items to long- and short-term items has as a general rule, one year of maturity. Regardless of the maturity of the items they can be also divided according to their liquidity. E.g. Stocks traded in the stock exchange are short-term financial assets because of their liquidity, while stocks not traded in a stock exchange are long-term assets (Bezrukih. 1996, 100).

3.2.2.1.2 Current assets

Current assets are also quite easily quantified, but the problem arises again in the valuation of inventories, in case the company is producing goods or services. If there is no production, the evaluation can be made using for example Replacement price method. For a manufacturing company, the evaluation of the stock of own production could be valued for example at the market price. The unfinished production can be valued according to the state of completeness in relation to the market price of the finished production. If the market price is used to evaluate the uncompleted production, one should diminish at least the assessed taxes from the market price or as in the case of Net realizable value, a normal mark-up (Hendriksen & van Breda 1991, 496). In Finnish accounting legislation the valuation of the production stock is based on the acquisition and production expenditure of the items in the stock. If the reacquisition value

of the product at the moment of evaluation is lower than the original value, the difference should be recorded as an expense (Järvinen et al.1998, 215). It is also possible include fixed costs of acquisition and production to the acquisition expenditure, when they are caused by the acquisition of this product, and are considerable in comparison to the variable costs (Järvinen et al.1998, 215). It is naturally possible to use the production value as the basis for the valuation of the current assets.

With the current fluctuations on the Russian currency, the safest method of valuation the materials and supplies stock might be LIFO or a replacement value. However, LIFO might give quite distorted value for the stock, although appropriate for pricing purposes. If the stocks are small, the meaning of the valuation method can be insignificant. The materiality of the valuation method is naturally proportional to the size of the stock in relation to the size of the company.

To analyse the content of the stock in an item level, there is a list of items introduced in Russian accounting called “Nomenklatura-Tsennik”. This item list has a 7 or 8 digit encoding to itemise every article in the stock. The 3 first digits on the codes have a similar structure as the chart of accounts, where the two first digits represent the synthetic account number and the third number denotes the sub account. The following one or two digits represent the group to which the article belongs to, and the rest are optional characteristics of the item itself (Bezrukih 1996,109).

Materials in the stock are traditionally divided into seven groups:

1. Raw materials and basic materials, which are defined to be the materials, that are used to manufacture the final product. The raw materials are the outcomes of rural economy and/or are natural recourses e.g. wheat, corn, etc. (grain), coal, ore, etc. The basic materials are outcomes of industrial production (flour, textiles, sugar, etc.).
2. Other materials, which have been defined as “Aiding” materials are materials that are used with raw materials, and that give the final product a certain characteristic, but which cannot be seen as a fundamental raw material (e.g. spices in the food industry). The used amounts of these materials usually are dependent of the amount basic materials used. Other materials are further itemised:
3. Fuel, for technological-, engine- and heating purposes
4. Freight materials.

5. Spare parts.
6. Bought semi-finished products.
7. Scrap and leftovers (e.g. sawdust).

A Russian entity has four alternative methods of inventory valuation (Baryznikov 1998, 349):

- Actual production value of each individual article.
- LIFO, where the articles are expensed according to the price of the latest batch arrived to the stock, until the overall amount is fulfilled.
- FIFO, where the articles are expensed according to the price of the first batch arrived to the stock, until the overall amount is fulfilled.
- Average price of the whole stock, which is the prevailing method.

Entity has a freedom to choose any of the above models, given that they have declared this method in their accounting policy (Bezrukih 1996, 112).

Receivables can be a more problematic area, in the sense, that Russian legislation does not allow the company to write off the uncertain receivables before the debtor has been bankrupted. If there are some obviously non-collectable receivables, these should be written off from the balance and into the income statement, as a bad debt expense, as they would be done e.g. in Finland.

Financing securities have no special interpretation when it comes to their value determination, unless the company has a large nominal amount of their own stocks. Revaluation of the own stock capital has the same structure of problems as all other items of fixed assets. Funds of consumption and accumulation, if annulled, become assets of this nature.

3.2.2.2 Liabilities

The Equity part of a western balance sheet is in Russian balance sheet under the third part, which is called Capital and Reserves. With an adequate amount of sub accounts there should not be any problems to address the equity items of the balance sheet. The most important account in this group is the account number 88 (account number 84 in the new chart of accounts) “Undistributed profit”. The account 88 has at least 5 sub accounts, which are used to

disclose the volume of the funds (88.3-5), Profit/loss of the accounting period (88.1) and the Profit/loss of the previous periods (88.2). Account 88 therefore represents the accumulated wealth, which the company has achieved during its total lifetime. The profit or the loss of a period is monthly entered to the account 88.1 credit in case of profit and debit in case of a loss (Bezrukih 1996, 426). Therefore at the end of the accounting period the credit balance at account 88.1 exhibits the accounting profit of the period. The account 89/96 is reserved for the future expenditure and payments, although seldom used. The equity as presented in the balance sheet consists of the same accounts as the 7th group³⁶ of the chart of accounts. The other accounts in the 7th group are (Sizov 2001, 157):

- 85 subscribed capital (80 in the new chart of accounts, name remains the same),
- 86 reserve capital (82 in the new chart of accounts, name remains the same),
- 87 additional capital (83 in the new chart of accounts, name remains the same):
 - 87.1 Revaluation reserve
 - 87.2 Emission income
 - 87.3 Valuables received free of charge.

Loan capital has to be naturally divided into a short term and to a long term financing. In Russian accounting the division criteria is 1-year maturity of the loan. The loans from credit institutions can be found from the account 92 when they are long-term loans and from the account 94 when they are short-term loans.

Advances received and trade payables are usually short-term finance, but for projects of longer duration they may also be long-term finance. However, they are recorded to the same sub accounts of 64 and 60 regardless the duration of the item. At the transition to the new chart of accounts the account 64 is closed and balance is moved to the account 62 (Sizov 2001, 88). Separate sub accounts for the account 62 are useful in resolving the difference between the items. Payables carried forward have to be collected from various accounts, which belong to the 6th and 7th group in the old chart of accounts³⁷.

³⁶ Group #8 at the old chart of accounts.

³⁷ See appendix number 4, balance sheet.

3.3 Some universally applicable performance evaluation figures

In Russian accounting there is a moderate variety of performance evaluation figures, some of which can be used as such. These figures should be used solely for performance evaluation purposes, so the person using this information should be well aware of all the possible differences in the accounting systems, and consequently, consider the results to be likely biased. The purpose of this chapter is to present few performance evaluation figures that can make use of original Russian accounting data. The advantage of the use of these performance evaluation figures is that they don't require additional work by the accountants.

The best figures are naturally those with the same technique of measurement on all of the elements of the calculation, e.g. stock turn or average time of storage. Stock turn is calculated based the Russian accounting data as follows (Kovalev & Patrov 1998,264):

In Russian:

Себестоимость реализации
Средние запасы

In English:

Production value of sales
Average stock (production value)

Here the measurement of the production value has no effect on the actual result, because the unit and the method of quantification of the factors in the formula are the same, but the result has a different unit of measure. Other usable coefficients might be e.g. Absolute liquidity (ability to make payments), turn on receivables or the structure of the loan capital. For a more comprehensive list of the usable performance evaluation figures, see appendix number 3.

Unfortunately, most of the more advanced performance evaluation figures require reassessment of the elements of the calculation (i.e. corrective calculations on the accounting material). For performance evaluation figures, comparability between entities and/or between evaluation dates could be seen as the most important requirement.

4 INFLUENCE OF THE CHANGES IN THE GENERAL PRICE LEVEL

Level of inflation is seldom considered to be among the most topical issues in the modern day accounting systems. Notwithstanding the current low inflation rates in western countries, there exist working standards for accounting in the economies of high inflation. The IAS provides two standards for reporting under high inflation, which are IAS standard 29 titled Financial Reporting in Hyperinflationary Economies and the IAS standard 15 titled Information reflecting the effects of changing prices. However, these standards have a common paradox. The IAS 29 presupposes a rather unusual state of economy where it is applicable, (e.g. Hyperinflation is indicated if cumulative inflation over three years is 100 per cent or more³⁸) and therefore it is very unlikely that IAS 29 would provide a comprehensive solution on different economies with eclectic sources of inflation. The IAS 15 requires that the valuation basis would be either general purchasing power or a current cost³⁹, which both would require rather accurate information about the inflation. In the Russian case the complication is quite evident, that of the absence of reliable price indices, such as CPI or PPI. The IAS standards on the other hand coerce the usage of price indices as an indicator of the magnitude of inflation and as a measure of the change in the price level. The case of the Russian Consumer Price Index was discussed earlier and the Producer Price Index for Manufacturing Industries (PPI) seems to have even less use for revaluation purposes: *"In the view of experts (Bessonov V.A.), errors in calculating the PPI are even greater than those in calculating the CPI. Due to significant errors in calculating price indices, there are doubts that their application will enhance the quality of financial disclosures."* (ICAR 2000, 1).

In the Russian case, usage of a general price level indices (CPI, PPI) to measure the rate of inflation is hardly advisable due to the consumption pattern changes, barter trading, and political influences, which all influence these indices. Another difficulty would be the existence of this data or the limited access to it. Also, if the inflation would be measured as a cost of living, hence the quantities would be taken into the equation of the general index, the inflation rate quantified this way would probably settle surprisingly low. In due time the error margin

³⁸ <http://www.iasc.org.uk>: IAS 29: Financial Reporting in Hyperinflationary Economies.

³⁹ <http://www.iasc.org.uk>: IAS 15: Information Reflecting the Effects of Changing Prices.

of these indices should settle to an acceptable level but in the interim, other solutions must be found to replace the above-mentioned methods. Despite the economic development there is still a need to apply the methods of inflation accounting: *“The economic environment of the Russian Federation still meets characteristics of hyperinflation as specified by IAS 29”* (ICAR 2000, 1).

In addition to the above-mentioned 100% rule, the IAS standard 29 provides three other indicators of hyperinflation:

- People prefer to keep their wealth in hard currencies or in non-monetary assets, local currency is held only to accommodate very short-term needs (Terehova 2000, 43).
- The general population regards monetary amounts not in terms of the local currency but in terms of a relatively stable foreign currency. Prices may be quoted in that currency (Deloitte Touche Tohmatsu. 2001, 44)
- Interest rates, salaries and prices are calculated to compensate the loss of value of money (Terehova 2000, 43).

The standard 15 is a standard to be used during price changes, but not during inflation, which is covered by the standard 29 (Kamyzanov 2000, 354). In general, all the argumentation supports the use of IAS standards, of which the IAS standard No 15 is already implemented in the Russian accounting standard number 4/99 (Terehova 2000, 221), but instead of the indices, Russians would prefer to use the exchange rate of some hard currency. For Example, on the case of the IAS 29 Terehova (2000, 45) states the following: “revaluation using the Central Banks rating of a foreign currency on the 1st of January of the year following the accounting period”. ICAR shares Terehova’s viewpoint on the currency rate as the method of revaluation and gives the same argumentation against the price indices that was already noted earlier in this paragraph: *“The case for the use of a hard currency in place of the national currency as a method of inflation accounting is its simplicity, objectivity and availability... Unlike indices whose values depend on their computation techniques, exchange rates are market driven”*(ICAR 2000, 1). In fact, it is not entirely accurate to claim that exchange rates were purely market-driven, because a large part of the exchange rate changes followed a political decision either by the Russian government or by the IMF.

4.1 Currency rate fluctuations

4.1.1 Reasons

The reasons for the economic crisis are naturally more extensive than the reasons of isolated change in the currency bid. However, in the Russian case the changes in the value of the domestic currency reflect public information about the changes in the economic environment with utmost accuracy. Without going deep into the structural problems of the Russian society, it is easy to endorse one of Mr. Stearns's comments about the needs of a successful capitalistic society: *"they must have a culture of honesty and respect for individuals and their property and they must have enforcement of the rule of law, and I think that is where it is falling down"*⁴⁰ More relevant and less overwhelming would be to discuss the events and conditions that led to the economic and politic turmoil at late 90's and gave rise to the financial crisis, such as: *"The direct cause of crisis has been the Russian government's failure to address fiscal imbalances."* (Cooper W. H., 2) The Russian budget had to be financed mainly by government bonds (so called GKO's) and other short term financing because the taxation could not provide the needed income.

Another government related reason is the inability to root out the corruption: *"The downfall of the ruble, as well as the weakening of so many Asian economies, is more related to corruption than to any other factor."*⁴¹ There is a general understanding of the reasons, but disagreement as to which are the most significant ones.

Among structural reasons on the financial markets, poorly structured banking system and the failure to create and institutionalise a favourable investment climate⁴² had an enormous effect when the currency flow to Russia turned negative. According to Komulainen (1999, 7): *"Increased capital mobility also meant increased financial instability"*, which quite well summarises the risks of the global capital, and when that risk realised in the prevailing economy the implications were quite severe.

⁴⁰ Representative Stearn at the *Examination of the Russian economic crisis and the international monetary fund aid package*. Thursday, September 10, 1998. p. 21. Originally from Michael Novak's book *"The Spirit of Democratic Capitalism"*.

⁴¹ U.S. House of Representatives 1998, 17.

⁴² U.S. House of Representatives 1998, 26.

The role of IMF in the Russian economic crisis was also a subject of a broad discussion. Although IMF was helping Russia to survive, the money that IMF gave to the Russian Central Bank did not find its way to where it was intended to go e.g. to unpaid wages etc. *“if other reports are true that as much as \$100 billion of the international aid to Russia has simply been transported out of the country to secure foreign accounts in Switzerland...”*⁴³ IMF has been accused of being naive in believing that economic reform is actually taking place. They should have required visible evidence from day one. On the other hand IMF pushed through some hard line capitalistic changes, but: *“The IMF prescribed that Russia run its economy for the benefit of foreign investors and a few wealthy Russians at the expense of the Russian people.”*⁴⁴ In this light it's not easy to categorise the Russian currency crisis on a microeconomic level, but it fits into the Asset market approach, described by Komulainen (1999, 17) as a theory where the exchange rate is determined by the investor's willingness to hold each currency. In a macroeconomic level there exists some signs of a contagious effect from the Asian crisis, predominantly through the changes in oil raw-material prices, but it doesn't imply exclusive causality to the inflation nor the economy because the effects were global.

The 17th of August 1998 was a day, which is usually considered as the starting point of the whole financial crisis:

The crisis came to a head on August 17, 1998, when the government of then-Premier Sergei Kiriyenko abandoned its defense of a strong ruble exchange rate against the dollar, defaulted on government domestic debt forcing its restructuring, and placed a 90-day moratorium on commercial external debt payments (Cooper W. H., 2).

This event was also considered to be Kiriyenko's personal failure for which he lost his office 6 days later. On the other hand, George Soros brought forward the exact same measure four days earlier (to devalue ruble). However, August 17th was the date when the exchange rate speculation really started to promote the financial crisis, and that brings us to the implications.

⁴³ U.S. House of Representatives 1998, 3.

⁴⁴ U.S. House of Representatives 1998, 5.

4.1.2 Implications

A strong disbelief to the banking sector, lack of bank savings, and the hoarding of dollars by the public easily undermined any effort by the central banks to uphold the currency rate bid for the rouble. Figure 2 illustrates the price of one USD in Russian roubles at the last third of 1998. The magnitude of the currency rate fluctuations was easily sufficient to make everybody interested in currency trading and –speculation.

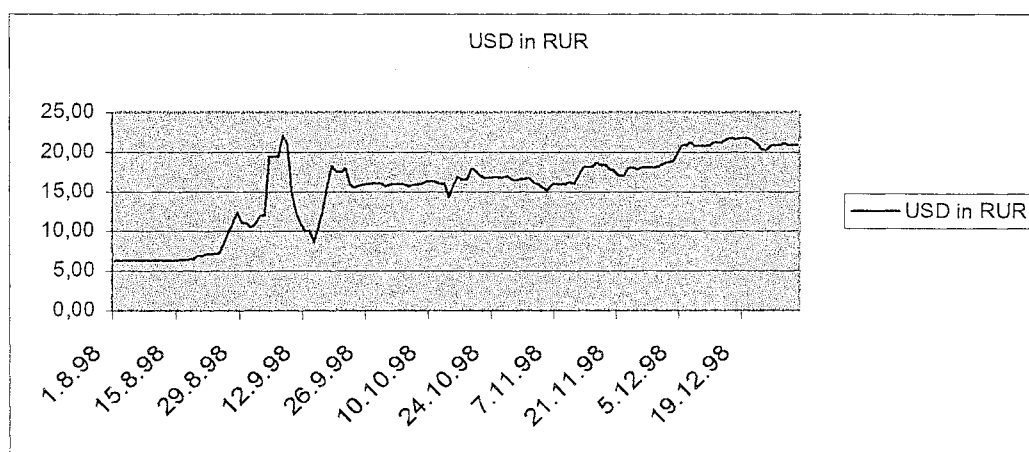


FIGURE 2 Value of one USD measured in RUR in the last third of 1998⁴⁵.

When it became obvious that the government had real problems repaying the bonds and GKO's, they needed to offer high yields (up to 135%) on these instruments in order to sell them. As a direct result the borrowing increased, as did the debt service expenditure, which was more 30% of the total Russian expenditure (Cooper, William H. 1999, 5).

Majority of foreign investors refused to roll over the bonds and treasury bills in the summer of 1998. With an average maturity of 11 months (Cooper, William H. 1999, 6), the foreign reserves were melting away fast. The reserves were augmented with IMF money in July 1998 but the relief was quite short, because the state could not defend the currency past August 17th 1998.

Failure to create and institutionalise a favourable investment climate brought on a new kind of sub economy where money seldom changed hands. The trading was performed by barter,

where goods were changed to other goods. By 1st of August 1998 there were 12.5 billion dollars of unpaid salaries owed to Russian workers⁴⁵. The only way to pay the salaries was with the products that the workers manufactured. This way of trading is naturally bad for the government, because it is inevitably inefficient to collect taxes in a form of products.

The collapse on the banking system took under a lot of small banks, but also the giant Inkombank. Many bank accounts, private and company accounts were frozen. In the bankruptcy of the Inkombank customers lost their savings, because there was not a government guarantee on their savings. The governmental Sperbank offered the Inkombank customers a nominal reimbursement of their savings, but by then nominal value of the savings was a fraction of the actual value when the accounts were frozen. The bankrupt's estates were then sold to another bank of the same consortium, and the same people continued business as usual in a bank that had an excellent economic state, since the debts remained in the bank under the old name.

⁴⁵ Source of the Exchange rate: The central bank of Russia.

⁴⁶ The Russian Financial Crisis: An Analysis of Trends, Causes, and Implications. p. 7.

5 INFLATION ACCOUNTING

Inflation, naturally, has effects on the outcomes of various accounting methods used to quantify and evaluate entity's performance and financial standing. Inflation can bias accounting data, which can result in numerous mistakes in decision-making; i.e. over optimism in the overall policy, overpayment of dividends, undersized replacement decisions, wrong pricing decisions, undersized insurances, and overpayment of bonuses (Goldsmith, Y. & Admon, K. 1977, 16). By choosing the right inflation accounting methods these effects can be controlled and rectified when necessary. Technique of inflation accounting affects allocation of resources, prices, wages, taxation and dividends. The nominal profit declared is not only a basis for taxation, but also an indication to employees of the value added that they are producing. If the nominal profit builds up on account of inflation, it can give rise to an unfounded wage claim by the personnel.

The inflation in the Russian economy is by no means due to the increases in the volume of the demand. These models, where the increased demand acts as the source inflation, usually apply to economies where an increase in the GNP foreruns the inflation. Russian GNP started to increase when the inflation had already started to settle. Therefore, a so-called demand-pull inflation is a somewhat inapplicable phenomenon to the Russian economy. With the last currency crisis the consumer prices on imported goods quadrupled in a few months, so it is needless to say that the consumption for the imported goods plummeted (especially daily consumer goods). Those consumers who still could afford imported goods make up a small fraction of the Russian population. The common middle and lower classes found the imported goods unattainable, or simply too expensive in comparison to the domestic products: *"Russian inflation in 90s was characterized not only by sky-rocketing prices but also by a significant change in price ratios. Prices for some products were rising at a rate that is several times higher than that for other products"*⁴⁷

For the reasons mentioned above, the consumption pattern in Russia has diverted from imported goods to domestic ones, and the prices of domestic production have actually devalued when measured in any hard currency. This development has brought out the most endorsed positive aspect of the currency crisis on the Russian

⁴⁷ ICAR newsletter: January/February 2000. Inflation accounting: Practices in different countries.

economy. The public media tends to see the growth of the GNP as a sign of a recovery in the national economy, and, to some extent, it is. Increase in the production is an answer to the increase in a demand on the lower price ranges (i.e. domestic products), but as long as the quality of the production is inferior to the foreign products, the lack of export possibilities makes the economy vulnerable to a trade gap in the future. For the first time in years the Russian government has reached a balanced government budget, which has the necessary funds to shorten the government debt. The reason for the increases in the government income is due to the high crude oil market prices. A more robust source for governmental income would be taxation, which unfortunately is not a realistic source to cover the expenditure in modern day Russia, as explained earlier. Now the Russian government is in a situation, where the world market price of crude oil determines the success of the Russian financial policy.

The literature about inflation and especially inflation accounting tends to be from the days when these issues were topical in western countries. However, the theories created then should be quite applicable for the Russian case, because the conceptual premises are the same.

5.1 Performance evaluation

5.3.1 Income

With a reasonable level of stability there are numerous ex ante definitions for income. Since this chapter concerns inflation and exchange rates, we shall not be concerned with expounding those definitions in detail, but will use a definition sufficient for this discussion.

The typical ex ante definitions of income all require prediction of the future to some extent. A typical ex ante approach would be: *“Income can be defined (by Hicks) as the maximum amount of money, which the person can consume during a period of time and be as well off at the end of that time as at the beginning”* (Hendriksen & van Breda 1991, 282). This income definition would at least require the prediction of the nominal value of the amount spent this week in the following week. Whilst the predicting of a one-week term would seem easy enough, it is seldom the time span used for financial accounting.

The prediction of the exchange rate seems to be quite difficult; therefore we will proceed straight to some of the variations of an ex post definition.

5.3.1.1 Consumption maintenance model

Applying the consumption maintenance model presented in Inflation accounting (Whittington 1983, 31-32) we arrive at the following method of calculating a periodical income:

$$V_0 = \sum_{t=1}^n \frac{Q_t}{(1+r)^t}$$

where V_0 = present value at time zero

Q_t = Cash receipts or payments at t periods

r = Discount rate per period.

The idea is that the income of a certain period is composed of the difference between opening net present value and closing net present value discounted to the time zero. If the cash receipt is not consumed and none of the expectations change, the net present value at time one can be calculated as follows:

$$V_1 = \sum_{t=2}^n \frac{Q_t}{(1+r)^{t-1}} + Q_1 = V_0(1+r)$$

Then the income of the period 1 can be quantified as the change between V_0 and V_1 .

$$Y = V_1 - V_0 = V_0 r$$

The difference between the Russian case, and the traditional demand-pull inflation cases is the source of inflation. When, for example, Whittington applies this formula, he assumes £1 to be £1 at the next point in time; only the purchasing power has been altered. Here the purchasing power has diminished, but because of the value changes in the measurement unit itself. Therefore V_1 should be discounted once more in order to get comparable figures, and reasonable results.

This approach works best when the r is relatively small, such as a consumer price index. However, since here the currency rate is defined the main source of inflation, and because almost all of the trading is valued in hard currencies, the discount rate should be quantified as the changes in the currency exchange rates.

Then $(1+r)^t$ could be quantified as $\left(\frac{C_t}{C_{t-1}}\right)$ where C_t is the currency exchange rate at time t .

Date	1.8.1998	1.10.1998	1.12.1998	1.2.1999
RUR/USD	6,28	15,95	18,60	22,77

TABLE 1 Price of one U.S. Dollar measured in Russian rouble since August 1998 through February 1st 1999.

A short and simple example with two periods might illuminate the usage of exchange rate as a discount factor. Assuming first target period to be from 01.08.1998 to 01.10.1998 and target period's cash flow to be 1.000.000 RUR, using the exchange rates in table 1, the first calculation forms as follows:

$$V_0 = \frac{1.000.000}{\left(\frac{15,95}{6,28}\right)} = 393730,40$$

Assuming the next period to be from 01.10.1998 to 01.12.1998, and the respective income to amount RUR 1.200.000, then the second calculation would take a following form:

$$V_1 = \frac{1.200.000}{\left(\frac{18,60}{15,95}\right)} + 1.000.000 = 2029032,25$$

Then the result of the second calculation should be discounted to the time zero, in order for the figures to be analogous:

$$V_1 = \frac{2029032,25}{\left(\frac{15,95}{6,28}\right)} = 798891,69$$

So the income for the target period, calculated as an increase in the net present value, formulates as follows:

$$Y = 798891,69 - 393730,40 = 405161,29$$

In this approach the fascinating feature is the effect that the future cash flows and discount

rate are determining this period's income. Actually this method is as ex post as they get, and therefore would benefit from noting that this period has an effect on the previous periods income. However, if the future prediction would be possible with acceptable likelihood, this method would save us from assessing any current values.

5.3.1.2. Constant purchasing power

Constant purchasing power can be used to calculate the profit, for example, in quite a similar fashion as the income in the previous paragraph. Starting with the opening balance at a moment of time t :

$$N_t + M_t \equiv L_t + P_t,$$

where N_t = Non-monetary assets at time t .

M_t = Monetary assets at time t

L_t = Liabilities at time t

P_t = Proprietors net worth at time t

The closing balance is then coherently:

$$N_{t+1} + M_{t+1} \equiv L_{t+1} + P_{t+1}$$

Restating the opening balance with Proprietors net worth as an indicator would be formed as follows:

$$P_t(1+p) = N_t(1+p) + M_t(1+p) - L_t(1+p),$$

where $(1+r)$ can be quantified $\left(\frac{C_t}{C_{t-1}}\right)$ where C is the currency rate.

Now it is possible to quantify the profit as the change in the value of P , assuming no transactions during the period. Before the profit can be calculated, the closing date balance must be re-evaluated to compensate for the value loss in the non-monetary assets:

$$P_{t+1} = N_t(1+p) + M_t - L_t$$

Since monetary assets and liabilities are already at monetary units, they should be left intact. Therefore, without any transactions the profit/loss is:

$$\Delta N_t(1+p) + M_t(1+p) - L_t(1+p)$$

So that only if the value of non-monetary assets changes deviating from $(1+p)$, the profit actually deviates from $P_t(1+p)$. When transactions are involved, the only precise method of producing the correct income figure is to stabilise each transaction individually. The discount rate is naturally available from the Russian Central bank on a daily basis.

5.3.2 Asset Valuation

Asset valuation is something that should be performed at some point in time, regardless of the climate surrounding the entity; Historical costs, even when the general index rests stable, must sooner or later cease to indicate the current values (Baxter 1984, 184).

Since the Russian accounting practice is balance orientated, the revaluation of the assets can offer the company a remarkable degree of additional information. As was discussed earlier, an item (for example, a stock lot) can have various different balance sheet- and nominal values.

To substantiate the problem, a short example would be in order. In this example the amount of the item in a stock is measured in two months interval. The amount of the item in stock at the moment of measurement is irrelevant as such, contrary to chosen valuation method, which determines the total value of the lot(s).

Units	Date	Replacement price /unit/RUR	Balance sheet value in RUR	Stock value in USD	Exchange rate RUR/USD	Replacement price /unit/USD	Historical price /USD
100000,00	1.8.1998	50,00	5000000	796178,34	6,28	7,96 USD	7,96 USD
80000,00	1.10.1998	55,00	4000000	250783,70	15,95	3,45 USD	3,13 USD
50000,00	1.12.1998	65,00	2500000	134408,60	18,60	3,49 USD	2,69 USD
90000,00	1.2.1999	70,00	4500000	197628,46	22,77	3,07 USD	2,20 USD

TABLE 2 Value of a certain lot measured in USD and RUR in the last third of 1998 ⁴⁸

Balance sheet value of the lot can be seen in the Value in RUR column. This is the true written down value recognised in the Russian accounting system. The nominal value of a unit in the stock has increased over time. Assume that the amount items in this lot A would have been down to 10.000 units before a new lot B arrived at 01.02.1999. The historical cost of the

remaining 10.000 units would be RUR 50 per unit, which would have been then USD 7.96 per unit, a total of 79600. With the exchange rate at 01.02.1999 of 22,77 it would be 22, 000 USD. In dollar terms, the replacement value of the old stock should be set to somewhere between 7,96 and 2,20. In this example the correct value in many cases would be the current replacement price at the current exchange rate, which would be 3,07 per unit in dollar terms, which is the average replacement price.

Most balance sheet figures are the sum of many entries at different dates with different price levels. Thus, more than one factor is in practice needed to revalue or stabilise each of these 'mixed' accounts (Baxter 1984, 49). Whilst the revaluated balance sheet might appear to be a summary of the evaluator's decision-making criteria, there are five soundly argued points in Baxter's book backing up the reasonableness of the evaluation:

1. Investment in shares. The analysts who evaluate companies like to use ratios to illustrate the performance of a certain company. Here the balance sheet figures usually play a key role. In Baxter's words: Without asset revaluation, they (balance sheet figures) must inevitably lose whatever virtue they may otherwise possess. They will lead to false comparisons between companies that vary in age and type (Baxter 1984, 185).
2. Creditor protection. Sound asset figures will help the creditors to assess the company's potential to meet their claims, and therefore protects the creditors against debtor's bankruptcy etc. Also, debtors can benefit from sound asset figures by getting better terms for their commitments towards the creditors.
3. Manager's appraisal of progress and new projects. The revaluated balance sheet (assuming it is done correctly) is naturally a much better basis for performance evaluation for the management, as well as being a better basis for assessing the profitability of future projects.
4. Insurance. The assessment basis for an insurance coverage is often the balance sheet items, which in monetary terms means the balance sheet value of those items.
5. Income measurement. The depreciations on the balance sheet items have a direct effect on the income statement; out-of-date balance sheet values can easily contribute to unrealised profit figures in the income statement.

Whittington's reasoning on behalf of accurate financial accounts is similar: A number of im-

⁴⁸ Source of the Exchange rate: The central bank of Russia. (www.cbr.ru)

portant decisions are based on financial accounts. Traditionally, these include management's decision to declare dividends, potential creditor's decision to offer finance to a company, investor's decision to buy (or sell) shares of the company, and shareholder's decision to support the present management by re-electing directors.

Net holding gains through restatements are profit in the Hicksian sense, but this profit concept necessitates the same level of inflation on the following periods. If the inflation is temporary, disclosing the profit might cause a problem: "it might be prudent to "neutralize" these inflationary gains to avoid raising income expectations...that cannot be fulfilled during non-inflationary years" (Goldsmith & Admon 1977, 32). The increase in the stock value should be seen as a holding gain rather than income, although according to Scott (1976): "*the real holding gains on stock depends upon the extend to which the increase in the real cost can be passed on the selling price*" (see Whittington, G. 1983, 112).

The performance measurement techniques and asset valuation both necessitate selection of the current value assessment system. There are various possible evaluation techniques for the current value, and we shall focus on the most significant ones.

5.3.2.1 Replacement cost

Replacement cost could be seen as the cost of the physical replacement of a certain asset in the evaluator's possession at the present moment. The possibilities to include acquisition costs in the value of the article are seldom without limit. When the endeavour is to produce realistic financial reports one should be careful not to include too much, if any, fixed costs in the replacement price. One basic principle to be followed is that purchases should not create unrealised holding gain, hence income, which is possible to do by, for example, overvaluing stocks with the last batch arrived.

When replacement cost is used to evaluate the results of the business activities in the income statement, the instant in time actually determines the ratio with which the realised gains are divided between holding gains and operating gains.

According to Goldsmith and Admon (1977, 49), replacement is justified only if the economic value of an asset exceeds its replacement costs. Even if the future cash flows (economic value) would be difficult to predict, this makes sense.

The information limit concerning the replacement cost is simple. When measuring values, the replacement cost reflects the costs of acquisition, and not necessarily the actual value of the article. The concept of net realisable value should reflect the actual value of the article more accurately.

5.3.2.2 Net realisable value

Valuing assets by net realisable value (NRV) is quite simple in theory. In practice it should be quite suitable to evaluate the stock on finished production. In general the net realisable value indicates the current cash equivalent of a certain article in the firms possession.

Therefore, for the usability of the NRV Whittington (1983, 124) states: “*Firstly, and probably most significant, is the usefulness of current NRV as an indication of an important opportunity facing the firm, that the disposing of asset*”. A second argument supporting NRV is on its measurement properties, especially additivity and objectivity. When valuing assets on the basis of NRV, there are at least two conflicts with certain accounting principles:

1. The first principle, which NRV violates, is the going concern principle. When the assets evaluated are not current assets but are factors of production, the intention should not be to sell them in the foreseeable future.
2. The second accounting principle, which NRV does not comply with, is the realisation principle. Although there is no transaction recorded, the NRV is still determined on the basis of an unrealised, imaginary business transaction.

5.3.2.3 Present Value

Present value is quantified on the basis of the future cash flows at the proper rate of discount. The problem associated with the present value is the prediction of the future cash flows, and in many cases, including the one covered here, the proper discount rate. In practice, the measurement of present values by accountants is regarded as too subjective to provide a reliable basis for accounting (Whittington 1983, 129). The usability of the present value becomes relevant in decision-making, etc. when the accuracy of the prediction is satisfactory for the decision-makers, and the discount rate is e.g. internal rate of return.

5.3.2.4 General price-level restatement

General price-level restatement is, by definition, the method closest to the constant purchasing power method of the earlier chapter. This method is also adopted by GAAP and the definition in Miller's GAAP guide states: "*The value of an asset restated in terms of current purchasing power*" (Williams 1994, paragraph 11 p. 5) Restating the asset values with current purchasing power is exactly the concept used earlier with a certain restriction. The changes in the actual purchasing power are somewhat problematic to measure in terms of indices due to the changes in the overall consumption patterns, so the currency rate related restatements could be seen to reflect the domestic currency's purchasing power when buying foreign currencies.

5.4 Depreciation and revaluation

The revaluation of a certain article naturally alters the corresponding valuation basis for the depreciation discussed earlier. When the valuation basis is altered, the depreciation method or its parameters should be adjusted accordingly. For example, for a linear depreciation method each revaluation makes a point of discontinuity on the value curve. Therefore if the scrap value of the item remains same, rate of depreciation either increases or decreases accordingly. The change in the depreciations should compensate the corresponding changes in the cash flow, when they are correctly quantified.

6 CONCLUSIONS

As we have established so far, Russian accounting contains numerous differences in comparison to say, Continental European accounting systems. Combined with the value variations caused by inflation these differences yield to a level, which should not be ignored by the end users of the accounting information.

Every user should evaluate the importance or materiality of these differences themselves (when applicable). If possible, the end user should determine whether there is a need for corrections. Many of the corrections are quite arbitrary, so they should be well argued. Unfortunately, there doesn't seem to be a way to obtain the needed information straight from the Russian annual Reports without making some adjustments. List of accounts used in company's bookkeeping is a considerable aid in understanding of the company's financial performance to those who have access to the accounting documentation of the company. Also the accounting policy can prove to be a very good tool in understanding the accounting system, especially since may itemise company specific depreciation and cost recognition methods.

Because most of the accountants have their own technique of recording of the bookkeeping entries, there is no reliable way to conclude a universal system of correspondence between the accounting entries and the items of the financial statements, so it is essential to understand the used recording system, and to use aggregate figures with caution.

Importance of explaining the fundamentals arises from two separate differences: First, the lack of concepts in general. There remain numerous concepts in Russian accounting, which are unclear to most of the accountants in Russia, especially to those, who haven't done any reporting based on western standards. These concepts are inherited from western accounting procedures, and sometimes applied wrongly. And secondly, deceiving closeness of two concepts, one Russian and one western. At first look e.g. matching Russian concept of purchases with Finnish concept of purchases might first deem unproblematic, but in order to follow accrual accounting for expense recognition one must use the sum of credit entries in the purchases account instead of debit entries, which the Russian accounting system acknowledges as purchases, because Russians postpone their expense recording until the purchased goods have been deployed in a production process.

In general, most of the entities facing the challenges caused by two dissimilar accounting systems do not need to run two separate accounting systems, but they can manage with the reports recalculated from the Russian accounting material. If the company has a Russian accounting professional implementing Russian accounting standards, this person should manage the reporting under that other accounting system as long as the content of the items are explained to this person well enough. If the accountant does not understand the basic concepts, he or she makes easily systematic errors with the reports.

Alternatively, for the decision making purposes we could use the uncorrected periodical report, just by paying more attention to the problematic areas. Someone, who knows the companies business and the meaning of the Russian annual reports, should deal with these problematic areas.

Summarizing the basic problems, which one encounters when composing a accounting report based on Russian accounting information, are:

- Russian accountants have constant problems meeting the reporting deadlines on account of difficulties getting the documentation on time to conclude the accounts for the period. One solution for this problem could be to explain, that these reports don't necessarily need the documentation verify the rightfulness of the report. Usually the Russian financial statements can't be completed before all the documentation has been handed to the accountancy. If the reporting has been done on the basis of the Russian accounting the only remaining option is to improve the handling of the invoices etc.
- The legislative boundaries for depreciations, expenditure recognition, tax reducible expenses etc. should be taken into consideration.
- Currency rate fluctuations and inflation causes some consideration mainly in the evaluation of assets, but also performance evaluation. Basically, the Dollar-rouble rate influences everything.
- Accounting should acknowledge the inflation as a continuous process. However its not very realistic requirement for the accounting of a small entity, so the devaluations done periodically should be performed with coherent system during- and between the accounting period(s).

When setting up a Russian accounting system, designed to comply multiple reporting standards, the list of accounts plays a key role. By choosing the right set of sub accounts (enough of sub accounts), the entity can have much better control over some of the most problematic items in the balance sheet. In order to get more detailed periodical reports; the entity should try to itemise following:

- Stocks, by the production state, by the type of product, materials by type, etc.
- Receivables, by causality, by duration, etc.
- Fixed acquisition costs of materials and products should be separated to their own account. This makes the evaluation of the stocks easier.
- If the entity chooses to use some other depreciation method than the norm given by in the taxation law, the depreciation difference should be recorded to a separate sub account.
- For consolidating purposes, the purchases should be divided to sub accounts in order to determine the relations between concern companies, hence the amount of internal trade.

When an entity is to determine the form of the reporting system, the pursued features of the system usually determine the complexity of the needed application. In this context it is vital to address the important features, and disregard those features, which don't necessarily bring any additional value, but just complicate the application. The factors, which should be considered when forming a system for reporting needs, could be as follows:

- How accurate reports we want from the system, i.e. what is the level of control.
- What kind of information is most beneficial (whether we concentrate on the balance sheet or income statement) and what kind of evaluation figures we should have.
- What is the information need of the interest parties (owners, investors, and creditors)
- What kind of resources do we have to answer the demands of the sought-after reporting standard (do we have the personnel / structural etc. resources to pursue the level of accuracy decided in the first point)
- Does our organisational structure support highly detailed accounting reports (i.e. the needed documentation available in time to make the reporting dates).

Some of the suggested measures, which should help the reporting and consolidating:

- Planning the list of the accounts as explained earlier.

- Choosing the correct accounting software. Especially this software's ability to comply Russian accounting standards.
- It also advisable to record the balance sheet values valued in some hard currency to secure the accuracy of the valuation of assets.
- Confirming the coherence of the accounting concepts between the personnel from different accounting environments (different institutes etc.).
- Setting accurate, but also realistic reporting dates. The dilemma of the delayed accounting documentation should not be ignored.
- Recruiting personnel, which is already familiar with the sought-after accounting standards.
- Emphasise the importance of the reporting, because Russian accounting personnel is easily very 'Russian accounting orientated'. Typically, if they are not obligated to do these reports, they will leave them undone.
- Clear and easily understandable written directions are the cornerstones of the whole system, this way the applications of own intuition does not bias the system.
- Build a system, which you understand yourself and which you therefore can also control.

Internal audit done by a Russian audit agency can help to avoid many unwanted surprises during a tax inspection or an external audit. While this does not necessarily help to achieve the reporting goals set here, the possible cost-benefit ratio of this audit is not to be ignored.

The future development of the Russian accounting should move towards IAS accounting standards. Although MinFin extended schedule of the accounting reform to reach year 2010, Russian accounting standards should be feasible much sooner. Thus far 14 standards are approved and 10 are under advisement; therefore one could expect to have quite comprehensive and feasible Russian accounting standards by the end of the year 2002.

Some of the accounting professionals are not very confident about the development of the Russian accounting system. Comments have been made about a connection between a complicated accounting system and a possibility to misuse the system. On another words, the people designing the system, like to keep the system complicated enough, to make it possible to take some advantages of the system.

However, recent development has been towards a more consistent accounting system, a sys-

tem that will soon be accessible even to those who exercise accounting solely on e.g. IAS standards. Recent changes in the accounting system have removed some of the most significant peculiarities of the old system, and presumably there will be more of this type of development in the future. At the moment a substantial reform in the tax codex would be a very welcome complement to accounting reform.

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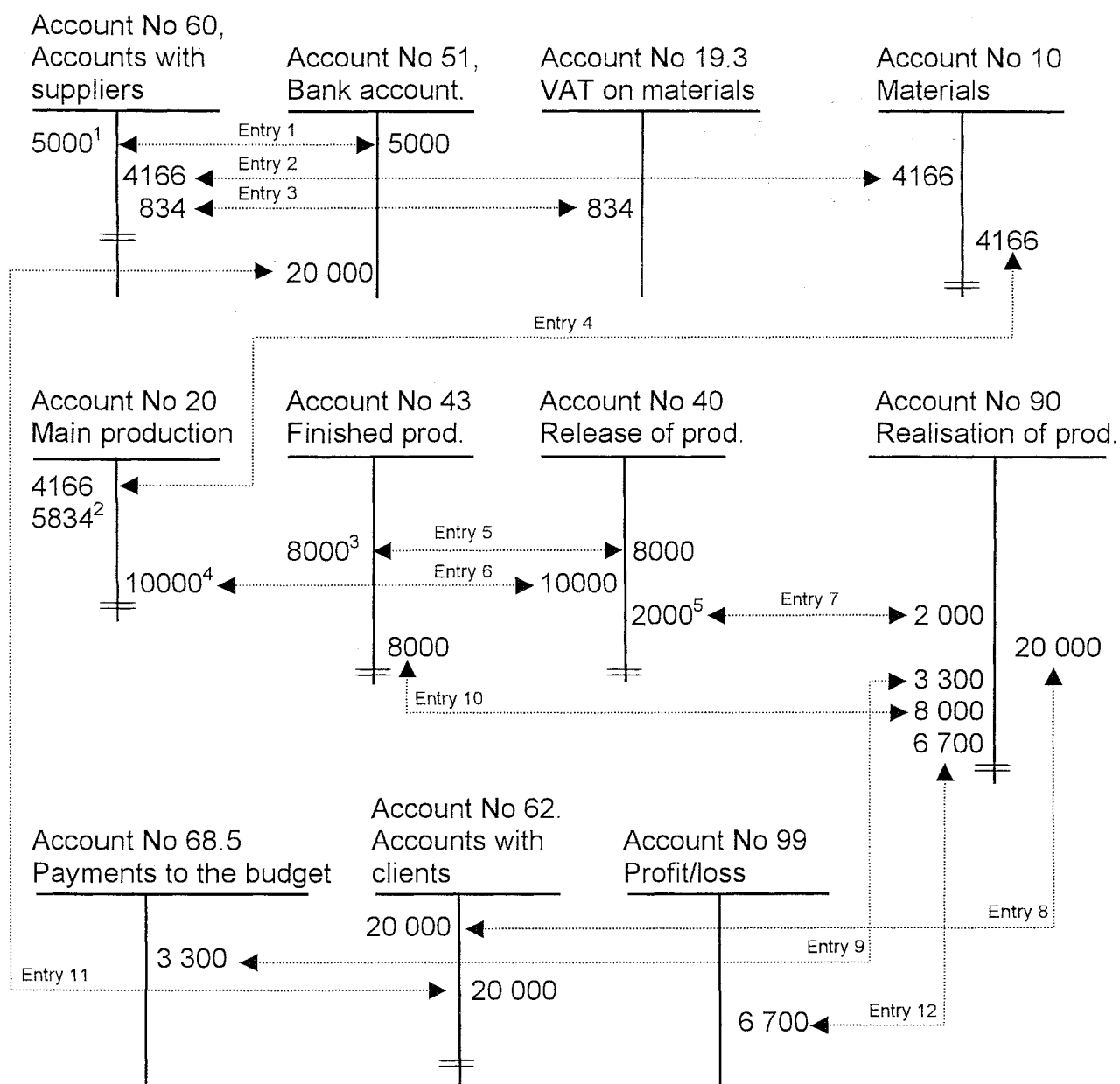
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Appendix 1. A simple example using the new chart of accounts.

¹ Buying price including VAT² Other manufacturing costs³ Estimated production value

⁴ Accurate production value (part of the balance on the account, quantified for the batch)

⁵ Difference between estimated and realised production value.

Appendix No 2: Documentation needed for Russian annual reporting.

Quarter balance

All this documentation is defined in the statute № 97 dated 12 November 1996, including instructions of filling these documents. The content of quarter balance is as follows:

- Balance sheet (*Бухгалтерский баланс, Балансовый отчет*).
- Income statement (*Отчет о прибылях и убытках*).
- Calculation of the assets in social security fund (*Расчетная ведомость по средствам фонда социального страхования Российской Федерации*).
- Report from the employer to the governmental organ of unemployment (*Обязательные сведения работодателя в Департамент федеральной государственной службы занятости населения по Санкт-Петербургу*).
- Calculation of average property of the company (*Расчет среднегодовой стоимости имущества предприятия*).
- Calculation of property taxes (*Расчет налога на имущество предприятия*).
- Quarterly calculation of the taxable income and tax advance withheld from physical persons employed (*Отчет об итоговых суммах начисленных доходов и удержанного подоходного налога с налогоплательщиков - физических лиц за 1 квартал, 1 полугодие, 9 месяцев, год*).
- Calculation of profit taxes (*Расчет налога от фактической прибыли за 1999 г*).
- Clarification of creditor organizations (*Перечень организаций-кредиторов по состоянию*).
- Clarification of debtor organizations (*Перечень организаций-дебиторов по состоянию*).
- Clarification of bank accounts in banks and other finance institutions in Russian soil (*Сведения о рублевых счетах в банках и иных кредитных учреждениях, действующих на территории Российской Федерации по состоянию на 1999 г*).
- Calculation of insurance payments to the Russian Federation Pension Fund (*Расчетная ведомость по страховым взносам в Пенсионный фонд Российской Федерации*).

- VAT calculation (*Расчет по Налогу на добавленную стоимость*).
- Calculation of mandatory medical insurance payments to the federal and territorial funds (*Расчетная ведомость по взносам в Федеральный фонды обязательного медицинского страхования*).
- Approval of tax reductions (*Справка о налоговых льготах*).
- Calculation of the road tax (*Расчет по налогу на пользователей автомобильных дорог*).

Statistics accounts.

Statistics accounts are a concise version of the quarter accounts. They have the same balance sheet, but the supplements needed are designed to give information merely for recording purposes.

- Information about production and shipping of products and services (*Сведения о производстве и отгрузке товаров и услуг*).
- Information of investments (*Сведения о инвестициях*).
- Information about the organisations financial state (*Сведения о финансовом состоянии организации*).
- Calculation of salaries of the workforce in the company (*Численность и начисленная заработная плата работников*).
- Information of production expenditure and Realisation of products (*Сведения о затратах на производство и реализацию продукции*).

Annual accounts include the same supplements as quarter accounts, and in addition to those mentioned above, the company has to include:

- Accounting policy (*Учетная политика организации*). Accounting policy states list of the accounts, valuations principles, valuation of imported goods, handling of exchange rate differences, usage of funds (pension fund etc.), and other principles, according to the nature of the business in question. Accounting policy has to be formed by head accountant, and approved by the management.
- Calculation of capital movements, form № 3 (*Отчет о движении капитала - форма N 3*)

- Cash flow statement, form № 4 (*Отчет о движении денежных средств - форма N 4*).
- Appendix to the balance sheet, form № 5 (*Приложение к бухгалтерскому балансу - форма N 5*). Form 5 includes clarification of: loan capital, trade receivables, trade payables, amortisation, long term investments, expenses, wins and losses of ongoing and previous year (period),
- Approval of the calculation method of the profit tax (*Справка о порядке исчисления строга I "Расчет налога от фактической прибыли"*)
- Calculation of taxes for the owner of a mean(s) of transportation (*Расчет по налогу на с владельцев транспортных средств*).
- Calculation of the tax on real estate funds and objects of social and cultural field. (*Расчет по налогу на жилищного фонда и объектов социально-культурной сферы*)
- Calculation of payments made to the legislative organs. (*Расчет сумм целевого сбора на содержание правоохранительных органов*)
- Calculation of the average amount of employees (*Расчет среднесписочной численности работников*).
- Calculation of advertising taxes (*Расчет налога на рекламу*).
- Approval of unrealised business transactions and missing objects liable to taxation (*Справка об отсутствии налогооблагаемых объектов и о неосуществлении ряда видов деятельности*).
- Itemisation of the calculation on wins and losses (*Расшифровка отчета о прибылях и убытках*).
- Clarification appendix (*Пояснительная записка*).
- Clarification of Russian currency bank accounts in banks and other finance institutions (*Сведения о рублевых счетах в банках и иных кредитных учреждениях, действующих на территории Российской Федерации по состоянию на 1999 г.*).

Appendix No 3.

We shall review here some of those figures that can be expected to be quite close to the “truth” and that might have some use on a decision making purposes. The aim is to illustrate a system, not to study the topic exhaustively.

The last formula on the right consisting of numbers tells the Russian balance sheet¹ lines, where the figures can be found.

1. Coefficient of quick liquidity.

Оборотные активы за минусом запасов	Current assets - stocks	с. 290 -с. 252 -с. 244 -с. 210 -с. 220 -с. 230
<u>Краткосрочные пассивы</u>	<u>Short time liabilities</u>	<u>с. 690</u>

The Russian term for this coefficient is: Коэффициент текущей ликвидности. The numbers on the right are the numbers of the lines in the balance sheet, where the figures should be taken from. This figure should not be biased due to an evaluation difference, because the items in it are not a subject of a revaluation in the entity. There is also a coefficient of liquidity, but it includes the value of the stock, which is the expected to bias the figure, as a result of undervalued stock.

2. Coefficient of absolute liquidity.

<u>Денежные средства</u>	Cash resources	с. 260
<u>Краткосрочные пассивы</u>	<u>Short time liabilities</u>	<u>с. 690</u>

This figure is also a one of those, which should not be disturbed by any evaluation choices made by the accountancy. Cash resources are simply cash money and money in the bank accounts i.e. liquid assets.

¹ These lines can be either in the actual balance or in some of its appendixes.

3. Turn on trade receivables²

<u>Выручка от реализации</u>	<u>Turnover</u>	<u>с. 010 *</u>
Средняя дебиторская задолженность	The average receivables	с. 240

The turnover of the Russian income statement corresponds quite closely to the western adaptation of turnover, and the trade receivables are valued with the market price. So the only potential factor influencing this figure might be the receivables, which would have been already written down in western adaptations of accounting and taxation procedures.

4. Stock turn

<u>себестоимость реализации</u>	<u>Production value of sales</u>	<u>с. 020 *</u>
средние запасы	Average stock (prod. value)	с. 210 +с.220

When the units on both sides of the formula are the same, the evaluation criterion of the unit has no effect on the result of the formula.

5. Profitability of the production.

(Рентабельность продукции)

<u>прибыль от реализации</u>	<u>Gains from the sales</u>	<u>с. 050 *</u>
выручка от реализации	Turnover	с. 010*

“Gains from the sales” is counted by deducting the production value of the sold production, commercial expenditure and administrative expenditure from the turnover. This figure is designed to present the profitability of the main business activities, and therefore it excludes the extraordinary incomes, -expenditure, financial items and the profit tax.

² * In the income statement.

6. Profitability of main activities

(Рентабельность основной деятельности)

<u>прибыль от реализации</u>	Gains from the sales	c. 050 *
<u>затраты на производство и сбыт продукции</u>	<u>Expenditure from production and from sales.</u>	<u>c. 020+c. 030 +c. 040*</u>

7. Coefficient of depreciation of assets

(Коэффициент износа основных средств)

<u>износа основных средств</u>	<u>Depreciation on assets</u>	c. 392 (г 4)
<u>Первоначальная стоимость основных средств</u>	<u>Original value of the assets</u>	<u>c. 371 (г 6)</u>

The numerals needed for this evaluation figure can be found appendix of the balance "form No 5". The number in the brackets indicates the column, where the corresponding numeral is. The possible usage of this evaluation figure could be to evaluate, how much out of line the Russian depreciation is in comparison to the company's general line.

Appendix No 4a.

INCOME STATEMENT (Old chart of accounts)

INCOME STATEMENT (Old chart of accounts)		1	2	1	2	1	2
		Account Number	Counter account	Account Number	Counter account	Account Number	Counter account
Sales							
	Sales, third party (+)	46 Credit	62 Debit	--	50 Debit	--	51 Debit
	Intermediate taxes (-)	68.2 Credit	46 Debit	68 Credit	46 Debit	67.1 Credit	46 Debit
TURNOVER							
Material, supplies and products							
	Purchases, third party (-)	60 Credit	10 Debit	--	41 Debit	--	19.3 Debit
	Purchases, group companies (-)	Determination by analysing the accounts above					
	Difference in rates (+/-)	C/D 83.4	--	C/D 80	Depending on the source		
	Other adjustments (+/-)	Usually included into purchases, can be found by analysing D 10.					
	Change in inventories(+/-)	41.2 Balance at the beginnin of the period - Balance at the end.					
	External services (-)	Usually included into purchases, can be found by analysing D 10.					
Personnel expenses							
	Salaries, employees (-)	(70 Credit-(opening balance -closing balance at 70) - 68.1-(0.01* 70 C)					
	Payroll tax (-)	68.1 Credit-(opening balance -closing balance at 68.1)					
	Pension, employees part 1% (-)	70 Credit * 0.01					
	Vacation salaries (-)	Separate sub accounts need to be formed in accounting					
	Payroll tax vacation salaries (-)	Separate sub accounts need to be formed in accounting					
	Pension vacation salaries (-)	Separate sub accounts need to be formed in accounting					
Social expenses							
	Pension, employers part 28% (-)	69.2 Credit	44 Debit				
	Social security 5,4% (-)	69.1 Credit	44 Debit				
	Medical security 3,4% (-)	69.3 Credit	44 Debit				
	Medical security 0,2% (-)	69.4 Credit	44 Debit				
	Unemployment insurance 1,5% (-)	69.5 Credit	44 Debit				
Depriciation							
	Depriciation, intangible assets (-)	05 Credit	44 Debit				
	Depriciation, buildings and construct. (-)	02 Credit	44 Debit				
	Depriciation, machinery and tools (-)	13 Credit	44 Debit				
Other operating costs		Analysing the account No 44 and 88 Debits, entries by definition.					
PROFIT / LOSS BEFORE FINANCIAL ITEMS							
Financial income							
	Dividend income (+)	Credit 80	Debit 78				
	Interest income (+)	Credit 80	Debit 51		Debit 94		
	Exchange profit (+)	Credit 80	Debit 60		Debit 76.1		Debit 52
	Other financial income (+)	Credit 80	Depending on the source				
Financial expenses							
	Interest expenses (-)	Debit 80	Credit 51				
	Increase in tax and interest of delay	Debit 80	Credit 68				
	Loan management expenses (-)	Debit 80	(Credit 94)				
	Exchange losses (-)	Debit 80	Credit 60.1		Credit 76.1		Cr.94 Cr.52
	Other financial expenses (-)	Debit 80	Depending on the source				
PROFIT / LOSS BEFORE EXTRAORDINARY ITEMS							
Extraordinary items							
	Extraordinary income (+)	Credit 48	(Debit 62)	Debit 47	(Debit 62)		
	Extraordinary expenses (-)	Debit 80	Those which by definition don't fall to other gatgories				
PROFIT / LOSS BEFORE RESERVES AND INCOME TAXES							
Increase or decrease in accelerated depriciation		Planned depriciation - Credit 02, 05, 13					
Change in voluntary reserves (+/-)		Change in the balance at 88.3, 88.4 and 88.5 (Maybe sometimes 89)					
Income taxes							
	Profit tax, final (-)	Debit 81	Credit 68.4				
	Other taxes (-)	Debit 80	Cr. 68.13		Credit 68.8		
	(Road tax, if not in turnover)	Debit 44	Credit 67.1				
PROFIT / LOSS FOR THE PERIOD							

Difference between external services and other operating expenses should be made in relation to the production.

Appendix No 4b.
BALANCE SHEET (Old chart of accounts)
ASSETS

Accounts

Fixed assets

Intangible assets	04				
Tangible Assets	01	07	08		
Financial assets	06				

Current assets

Valuation items					
Raw materials	10	11	12	15	
Work in progress	20	21	23	29	30
Finished goods	40				
Other stocks	41				
Advance payments	61				
Receivables					
Sales receivables	62	45	76		
Loan receivables	73	76			
Receivables carried forward	31	61	65	67	68
	69	70	71	75	78
Other receivables	73	76	78		
Stocks and shares	58				
Cash and bank deposits	50	51	52	55	56
	57				

LIABILITIES

Equity

Restricted capital					
Subscribed capital	85				
Revaluation reserve	86				
Other capital	87	88.3	88.4	88.5	
Non-restricted capital					
Retained earnings/accumulated loss	88.2				
Profit/loss for the period	87.1				
Obligatory reserves					
Expense reserve	82				
Other reserves	89				

Foreign capital

Non-current (long term)

Loans from credit institutions, non-curre	92				
Advances received	64				
Trade payables	60				
Other con-current liabilities	93	95			

Current (short term)

Loans from credit institutions, current	90				
Advances received	64				
Trade payables	60				
Payables carried forward	65	67	68	69	70
	75	76	78	83	
Other current liabilities	93	93			

INCOME STATEMENT (New chart of accounts)

INCOME STATEMENT (New chart of accounts)		1	2	1	2	1	2
		Account Number	Counter account	Account Number	Counter account	Account Number	Counter account
Sales							
	Sales, third party (+)	90 Credit	62 Debit	--	50 Debit	--	51 Debit
	Intermediate taxes (-)	68.2 Credit	90 Debit	68 Credit	90 Debit	67.1 Credit	90 Debit
TURNOVER							
Material, supplies and products							
	Purchases, third party (-)	60 Credit	10 Debit	--	41 Debit	--	19.3 Debit
	Purchases, group companies (-)	Determination by analysing the accounts above					
	Difference in rates (+/-)	C/D 98.4	--	C/D 99	Depending on the source		
	Other adjustments (+/-)	Usually included into purchases, can be found by analysing D 10.					
	Change in inventories(+/-)	41.2	Balance at the beginnin of the period - Balance at the end.				
	External services (-)	Usually included into purchases, can be found by analysing D 10.					
Personnel expenses							
	Salaries, employees (-)	(70 Credit-(opening balance -closing balance at 70) - 68.1-(0.01* 70 C)					
	Payroll tax (-)	68.1 Credit-(opening balance -closing balance at 68.1)					
	Pension, employees part 1% (-)	70 Credit * 0.01					
	Vacation salaries (-)	Separate sub accounts need to be formed in accounting					
	Payroll tax vacation salaries (-)	Separate sub accounts need to be formed in accounting					
	Pension vacation salaries (-)	Separate sub accounts need to be formed in accounting					
Social expenses							
	Pension, employers part 28% (-)	69.2 Credit	44 Debit				
	Social security 5,4% (-)	69.1 Credit	44 Debit				
	Medical security 3,4% (-)	69.3 Credit	44 Debit				
	Medical security 0,2% (-)	69.4 Credit	44 Debit				
	Unemployment insurance 1,5% (-)	69.5 Credit	44 Debit				
Depriciation							
	Depriciation, intangible assets (-)	05 Credit	44 Debit				
	Depriciation, buildings and construct. (-)	02 Credit	44 Debit				
	Depriciation, machinery and tools (-)	10.9 Credit	44 Debit				
Other operating costs		Analysing the account No 44 and 88 Debits, entries by definition.					
PROFIT / LOSS BEFORE FINANCIAL ITEMS							
Financial income							
	Dividend income (+)	Credit 99	Debit 76.x	For 76.x processing rules yet unestablished			
	Interest income (+)	Credit 99	Debit 51		Debit 66		
	Exchange profit (+)	Credit 99	Debit 60		Debit 76.1		Debit 52
	Other financial income (+)	Credit 99	Depending on the source				
Financial expenses							
	Interest expenses (-)	Debit 99	Credit 51				
	Increase in tax and interest of delay	Debit 99	Credit 68				
	Loan management expenses (-)	Debit 99	(Credit 66)				
	Exchange losses (-)	Debit 99	Credit 60.1		Credit 76.1		Cr.66 Cr.52
	Other financial expenses (-)	Debit 99	Depending on the source				
PROFIT / LOSS BEFORE EXTRAORDINARY ITEMS							
Extraordinary items							
	Extraordinary income (+)	Credit 91	(Debit 62)				
	Extraordinary expenses (-)	Debit 99	Those which by definition don't fall to other gatgories				
PROFIT / LOSS BEFORE RESERVES AND INCOME TAXES							
Increase or decrease in accelerated depriciation		Planned depriciation - Credit 02, 05, 13					
Change in voluntary reserves (+/-)		Change in the balance at 88.3, 88.4 and 88.5 (Maybe sometimes 96)					
Income taxes							
	Profit tax, final (-)	Debit 99	Credit 68.4				
	Other taxes (-)	Debit 99	Cr. 68.13		Credit 68.8		
	(Road tax, if not in turnover)	Debit 44	Credit 68				
PROFIT / LOSS FOR THE PERIOD							

Difference between external services and other operating expenses should be made in relation to the production.

Appendix No 4d.**BALANCE SHEET (New chart of accounts)****ASSETS**

Accounts

Fixed assets

Intangible assets

04

Tangible Assets

01

07

08

Financial assets

58

Current assets

Valuation items

Raw materials

10

11

15

Work in progress

20

21

23

29

30

Finished goods

40

Other stocks

41

Advance payments

60

Receivables

Sales receivables

62

45

76

Loan receivables

73

76

Receivables carried forward

97

60

76

68

69

70

71

75

Other receivables

73

76

Stocks and shares

58

Cash and bank deposits

50

51

52

55

57

LIABILITIES**Equity**

Restricted capital

Subscribed capital

80

Revaluation reserve

82

Other capital

83

84.3

84.4

84.5

Non-restricted capital

Retained earnings/accumulated loss

84.2

Profit/loss for the period

83.1

Obligatory reserves

Expense reserve

63

59

Other reserves

96

Foreign capital**Non-current (long term)**

Loans from credit institutions, non-curre

67

Advances received

62

Trade payables

60

Other con-current liabilities

95

66

67

Current (short term)

Loans from credit institutions, current

66

Advances received

62

Trade payables

60

Payables carried forward

98

68

69

70

75

76

76.1

Other current liabilities

66

67

Appendix 5 New chart of accounts (effective from January 1st. 2001)

Part 1. Non-current assets

First Capital	01
Amortisation of First Capital	02
Assets producing revenue	03
Intangibles	04
Amortisation of Intangibles	05
Equipment under installation	07
Acquisition of non-current assets	08

Part 2. Current assets (production stock)

Materials	10
Domestic and farm animals	11
Reserve for a decrease in value of the stock	14
Manufacturing and acquisition of tangibles	15
Fluctuations in the price of tangibles	16
VAT on purchases	19

Part 3. Production expenditure

Core production	20
Semi-finished production	21
Supporting production	23
Production overhead	25
General overhead	26
Scrap from production	28
Helping functions	29

Part 4. Finished productions and inventories

Release of production	40
Inventories	41
Sales discounts	42
Finished production	43
Sales expenditure	44
Goods en route	45
Partial debiting	46

Part 5. Monetary assets

Cash	50
Bank account	51
Currency account	52
Special bank accounts	53
Exchanges en route	54
Financial assets	58
Reserves securing the value of securities	59

Part 6. Financial items

Accounts with suppliers	60
Accounts with clientele	62
Credit loss provision	63
Short-term credit and loans	66
Long-term credit and loans	67
Taxes and levies	68
Social security and pensions	69
Salaries to personnel	70
Accounts with responsible employees	71
Accounts with personnel	72
Accounts with proprietors	73
Accounts creditors and debtors	74
Inter-company accounts	79

Part 7. Capital

Basic capital	80
Share capital	81
Reserve capital	82
Additional capital	83
Retained profit	84
Predetermined financing	86

Part 8. Financial results

Sales	90
Other income and expenditure	91
Partial losses on valuables	94
Future consumption reserve	96
Accrued expenses	97
Accrued income	98
Gains & losses	99