

Diagnostic Study of Accounting and Auditing Practices in Azerbaijan

Prepared Under Regional Technical Assistance (RETA)
5980: *Diagnostic Study of Accounting and Auditing Practices
in Selected Developing Member Countries*

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Preface

This report was prepared under Regional Technical Assistance (RETA) 5980: *Diagnostic Study of Accounting and Auditing Practices in Selected Developing Member Countries* for the Asian Development Bank (ADB) by Francis B. Narayan, Lead Financial Management Specialist, ADB; Sarath Lakshman Athukorala, Financial Management Specialist, ADB; Barry C. Reid, Consultant, ADB and Nailya Ablieva, Elmir Gasimov (Director) and Velieva Kenul (Office Manager) of Eligible Research Agency (ERA) Ltd provided excellent research assistance and logistical support.

The report describes Azerbaijan accounting and auditing arrangements, identifies deficiencies in those arrangements, and presents recommendations to address those deficiencies. It is part of the ADB series of country Diagnostic Studies of Accounting and Auditing (DSAAAs). In 2000, DSAAAs were completed and published for Cambodia, Mongolia, Pakistan, Papua New Guinea, People's Republic of China, Uzbekistan and Viet Nam. In 2001-02, DSAAAs were prepared for five further countries, including Azerbaijan.

The contents of the draft report were discussed and debated with representatives from the Government, the private sector and international organizations at a workshop held at Baku on 5-6 December 2001. The issues and recommendations were further discussed at an international workshop at ADB headquarters in Manila on 5-6 March 2002.

This report should be read in conjunction with the Summary Report, which identifies and examines selected issues in relation to accounting and auditing.¹

The authors would like to offer their appreciation to the officials and agencies that gave up their valuable time and made materials available during the course of the research. In particular we would like to thank Marco Gatti (Senior Programs Officer, ADB) and Faraj Huseynbeyov (ADB Liaison Officer in Azerbaijan) for their support and Kunio Senga (Director, Operations Coordination Division, East and Central Asia Department, ADB) and Neside Tas-Anvaripour (Financial Management Specialist, ADB) for moderating the Manila workshop session at which this report was discussed.

Our special appreciation is to Abbas Allahverdiyev (Deputy Chair, Azerbaijan Chamber of Accounting), Elkhan Jafarov (Head, Accounting

¹ ADB. 2002. *Accounting and Auditing Practices in Selected Developing Member Countries: A Diagnostic Study of Azerbaijan, Fiji Islands, Marshall Islands, Philippines and Sri Lanka*. Manila: ADB.

Policy Department, Azerbaijan Ministry of Finance), Professor Vahid T. Novruzov (Chair, Chamber of Auditors of Azerbaijan) and Ismailiyov Sabir (Former Chair of the Accounting Policy Department, Ministry of Finance) for their support of the study, and for their involvement in the Baku and Manila workshops.

The World Bank is undertaking a coincident Country Financial Accountability Assessment (CFAA). The CFAA exercise, although broadly similar to this DSAA, involves multiple missions and will extend over a period of months. The CFAA will provide the basis for discussions with the Government regarding the World Bank Second Structural Adjustment Credit (SAC-2). Drafts of this DSAA report were shared with the World Bank mission in December 2001, January 2002 and February 2002.

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ADB Diagnostic Studies of Accounting and Auditing

The Asian Development Bank (ADB) publishes this series to: (i) provide reference materials on accounting and auditing for government officials, ADB officials, officials from other donor agencies, and other interested parties; (ii) identify potential actions that the participating government and / or the accounting profession can take to rectify weaknesses, in partnership with donor agencies where appropriate, and (iii) provide the participating country with a benchmark against which to measure their progress in improving financial management and governance arrangements.

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Summary Reports

Accounting and Auditing Practices in Selected Developing Member Countries (DMCs): A Diagnostic Study of Azerbaijan, Fiji Islands, Marshall Islands, Philippines and Sri Lanka. 2002.

Financial Management and Governance Issues in Selected Developing Member Countries (DMCs): A Study of Cambodia, People's Republic of China, Mongolia, Pakistan, Papua New Guinea, Uzbekistan, and Viet Nam. 2000.

Individual Reports: By ADB Region

All ADB DMCs are listed by region. Economies for which a DSAA has been prepared are bolded and the year of publication is shown in brackets:

East and Central Asia: **Azerbaijan** (2002); **People's Republic of China** (2000); Hong Kong, China; Kazakhstan; Kyrgyz Republic; Republic of Korea; **Mongolia** (2000), Tajikistan; Taipei, China; Turkmenistan; and **Uzbekistan** (2000).

Mekong: **Cambodia** (2000), Lao People's Democratic Republic, Myanmar; Thailand, **Viet Nam** (2000).

Pacific: Cook Islands, Democratic Republic of East Timor, **Fiji Islands** (2002), Kiribati, Republic of the **Marshall Islands** (2002), Federated States of Micronesia, Nauru, **Papua New Guinea** (2000), Samoa, Solomon Islands, Tonga, Tuvalu, Vanuatu.

South Asia: Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, **Pakistan** (2000), **Sri Lanka** (2002).

Southeast Asia: Indonesia, Malaysia, **Philippines** (2002), Singapore.

CURRENCY EQUIVALENTS

(as of 18 February 2002)

Currency Unit – Azerbaijan Manats (AZM)
AZM1.00 – \$0.0002079
\$1.00 – AZM4,810

ABBREVIATIONS

| | |
|----------|--|
| AAC | Azerbaijan Accounting Chamber |
| ABTC | Azerbaijan Banking Training Center |
| ACAAz | Association of Certified Accountants of Azerbaijan |
| ADB | Asian Development Bank |
| BAFS | Broadly Adapted Financial Statement |
| CAP | Country Assistance Plan |
| CFAA | Country Financial Accountability Assessment |
| CIS | Commonwealth of Independent States |
| COAA | Chamber of Auditors of Azerbaijan |
| COS | Country Operational Strategy |
| CPA | Certified Public / Practising Accountant |
| CPE | Continuing Professional Education |
| DMC | Developing Member Country |
| ED | Exposure Draft |
| EU-TACIS | European Union - Technical Assistance for the Commonwealth of Independent States |
| FSU | Former Soviet Union |
| GDP | Gross Domestic Product |
| GNP | Gross National Product |
| IAPC | International Auditing Practices Committee |
| IAPS | International Auditing Practice Statement |
| IAS | International Accounting Standard |
| IASB | International Accounting Standards Board |
| IASC | International Accounting Standards Committee |
| IDP | Internally Displaced Person |
| IEG | International Education Guideline |
| IES | International Education Standard |
| IFAC | International Federation of Accountants |

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|------------------|---|
| IFRS | International Financial Reporting Standard ² |
| IRFAA Eurasia | International Regional Federation of Accountants and Auditors (IRFAA) Eurasia |
| IIA | Institute of Internal Auditors |
| IMF | International Monetary Fund |
| INTOSAI | International Organization of Supreme Audit Institutions |
| IOSCO | International Organization of Securities Commissions |
| IPSAS | International Public Sector Accounting Standard |
| ISA | International Standard on Auditing |
| ISAR | Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting of the UNCTAD |
| JBIC | Japan Bank for International Cooperation |
| JICA | Japan International Cooperation Agency |
| MOED | Ministry of Economic Development |
| MOF | Ministry of Finance |
| MTEF | Medium-Term Expenditure Framework |
| NBA | National Bank of Azerbaijan |
| NGO | nongovernment organization |
| OECD | Organisation for Economic Cooperation and Development |
| PSA | Production Sharing Agreement |
| PSC | Public Sector Committee |
| RETA | Regional Technical Assistance |
| ROSC | Report on the Observance of Standards and Codes |
| SAI | Supreme Audit Institution |
| SME | Small or Medium Enterprise |
| SOE | State-owned Enterprise |
| SPC | State Privatization Committee |
| STA | State Tax Administration |
| TA | Technical Assistance |
| UAS | Uniform Accounting System |
| UN | United Nations |
| UNCTAD | United Nations Conference on Trade and Development |
| UNDP | United Nations Development Programme |

² In 2001, the International Accounting Standards Board (IASB) assumed responsibility from the International Accounting Standards Committee (IASC) for promulgating IASs. In future, IASB-issued standards will be called International Financial Reporting Standards (IFRSs). Although the IASB now expects its standards to be called IFRSs, this report uses the term IASs (in the interests of continuity).

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| US | United States |
| USAID | United States Agency for International Development |
| WTO | World Trade Organization |

Notes

- (i) The fiscal year of the Government ends on 31 December. 'FY' before a calendar year denotes the year in which the fiscal year ends.
- (ii) In this report, \$ refers to US dollars.

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Executive Summary

Background

Azerbaijan is located in the South Caucasus region, on the western shore of the Caspian Sea. In the 19th century, it experienced an unprecedented oil boom and—by 1900—was supplying almost half of the world's oil.

This oil-rich country's population of about 8 million comprises different ethnic groups, including Azeris, Dagestanis and Russians. It gained independence from the Soviet Union in 1991 amid war and political turmoil—a 1994 ceasefire agreement ended an armed conflict with Armenia. However, about one-seventh of Azerbaijan's territory remains occupied, while around 800,000 refugees and internally-displaced persons are scattered throughout the country. Almost 70 percent of the population lives in poverty.

In 1994, Azerbaijan signed a 30-year contract worth \$7.4 billion with a British Petroleum-led consortium. A number of production-sharing arrangements have since been negotiated with foreign firms, which have thus far committed \$60 billion to oil field development. Oil production under the first production-sharing agreement began in November 1997.

Azerbaijan shares all the problems of other Former Soviet Union (FSU) countries, but its economic reforms were delayed by the unstable domestic situation. Since the mid-1990s, it has made progress towards establishing a market economy and restoring macroeconomic stability. A privatization program was introduced in September 1996. Within three years, over 21,000 small enterprises had passed into private hands. Inflation of 1,500 percent in 1994 was reduced to just 2 percent in 2001.

Overall economic performance has been consistently strong—real GDP growth for 2001 was estimated at 9.9 percent. However, this growth is concentrated in the oil and oil-related sectors. Other sectors remain weak and unemployment was estimated at 18 percent in 2000.

The unresolved conflict impedes economic progress and deters foreign investment. Long-term prospects depend upon world oil price levels, the location of new regional pipelines and Azerbaijan's ability to manage its oil wealth. Maintaining the competitiveness of non-oil exports is a serious long-term challenge.

Challenges and Responses

The Government established the State Oil Fund—an intergenerational trust fund—in November 1999. The Fund will enable better management of oil revenues. Progress has also been made in implementing policy reforms, such as the passage of the *Civil Code* (effective 1 September 2000) and the amended *Tax Code 2000* (effective 1 January 2001). However, structural reforms, particularly in the banking sector, have lagged behind. Crucial reforms are needed in this sector to improve supervision and strengthen enforcement of prudential regulations in line with international best practice.

The amended *Tax Code 2000* is expected to increase fiscal revenues. However, increasing social expenditures while maintaining fiscal discipline remains a challenge, as does managing projected oil revenues and developing the non-oil sectors.

To maintain investor confidence, government will need to implement structural reforms, including privatization, financial sector restructuring, and the establishment of institutions and the rule of law that are conducive to a market-based economy.

The principal elements of government's medium-term strategy include: (i) maintaining fiscal and monetary policies that support macroeconomic stability; (ii) implementing aggressive programs to strengthen energy sector governance and financial discipline; (iii) maintaining the liberal trade regime; (iv) accelerating structural reforms; and (v) implementing measures that will improve the legal and regulatory environment for private sector development.

A comprehensive anticorruption program is being developed as part of government's overall effort to enhance governance. To this end, the Azerbaijan Accounting Chamber (AAC)—Azerbaijan's Supreme Audit Institution (SAI)—has been established. The AAC has the authority to audit all government bodies, including all budgetary and extra-budgetary organizations and funds, and will publicly report its findings.

Accounting and Auditing in Azerbaijan

Azerbaijan developed its Soviet-based accounting system throughout the 1920s and 1930s. The 'Soviet accounting system' catered to the needs of central planning, in particular, the system provided accounting information, including: (i) financial information; (ii) tax information; and (iii) statistical information. It emphasized standardization and uniformity so that information could be compared across sectors and industries.

Upon independence in 1991, Azerbaijan found itself in the same position as other Former Soviet Union (FSU) countries concerning accounting arrangements. However, the Soviet accounting system created a sound basis on which to build. The system used many concepts of modern accounting including accrual measurement and double entry bookkeeping. Furthermore, large numbers of bookkeepers were trained in these concepts and were proficient in their application.

In the decade since the beginning of the transition, Azerbaijan has made some progress in developing an accounting infrastructure suitable to the needs of a market economy. However, financial management reforms were slow-tracked due to emphasis on the conflict and development of the oil and gas sector. Consequently, Azerbaijan's accounting and auditing reforms lagged behind those of many other FSU countries.

Articles 120–125 of the *Civil Code 1999* govern accounting and auditing arrangements in Azerbaijan. In particular, the *Civil Code 1999* stipulates the structure of Azeri financial statements. The Ministry of Finance (MOF) administers the *Law on Accounting 1995*, which regulates the maintenance of accounting records and the preparation of balance sheets by business entities and organizations in both the private and the public sectors. It also sets out financial reporting requirements. Other relevant laws include the *Joint Stock Companies Law 1994*, the *Enterprises Law 1994*, the *Banking Law 1996* and the *Tax Code 2000*. These laws conflict in places regarding accounting and reporting arrangements. At the same time, the prescriptive nature of the *Civil Code 1999* conflicts with the flexible provisions of the *Tax Code 2000*.

The main reporting requirements for legal entities are the quarterly tax return and statutory annual accounting reports that are filed in March–April. The accounting arrangements for relevant foreign companies usually exempt these companies from following Azeri accounting practices. The MOF has prepared a five-year program to develop accounting practices. This program is currently being considered and covers legislation, accounting standards, certification, ethics and training.

Auditing in the FSU reflected the highly controlling nature of the underlying accounting system. It was primarily a verification exercise, with the final accounts being compared to the bookkeeping records by accountants from another enterprise, or from the control and revision board. Moreover, with the state undertaking controlling, crediting and investment functions, there was no need for a fully functioning audit profession. The auditing profession has only been created within the short time frame of 10 years.

The *Auditing Services Law 1995* governs auditing activities in Azerbaijan. Other laws stipulate audit requirements. In general, all organizations must be audited. The *Auditing Services Law 1995* describes the 'Audit Conclusion' as an estimation of an organization's financial state. As of April 2001, 160 individuals and 32 firms were licensed to conduct audits in Azerbaijan (five of these firms were foreign).

Professional Infrastructure

The Soviet accounting system required neither professional accountants nor an accountancy profession. This changed with Azerbaijan's transition to a market economy, following independence in 1991.

The Chamber of Auditors of Azerbaijan (COAA) began operations in 1996 in accordance with the provisions of the *Auditing Services Law 1995*. Under these provisions, the Chamber is responsible for: (i) overseeing auditing activities in Azerbaijan; (ii) issuing auditing instructions, standards and guidance; (iii) licensing individual auditors and auditing firms; (iv) considering complaints against individuals and auditing firms; (v) consulting the profession on relevant legislative issues; (vi) reviewing the compliance of foreign individuals and foreign audit firms with the *Auditing Services Law 1995*; and (vii) conducting audits. The COAA may also establish auditing firms and, until January 2001, it also conducted fee-paying audits on its own behalf in competition with its members.

The Supreme Council of Azerbaijan appoints the Chamber's Chairperson and Deputy Chairperson. Individual auditors and auditing firms are required to pay membership fees to COAA. The Chamber holds memberships in several international and regional bodies, including those for SAIs, but it will be relinquishing the SAI memberships in favor of the recently established AAC.

As of April 2001, the COAA had issued renewable five-year audit licenses to 160 individuals, 27 local firms and five foreign firms. Auditing firms must comprise at least three qualified individuals. Individuals must be Azerbaijan citizens, although the Chamber may accept the qualifications of foreigners, who are licensed to practice in their own countries. To qualify for an audit license, individuals must: (i) have completed higher education in accounting, finance, economics or law; (ii) pass the auditor's license examination set by a COAA-appointed Commission; and (iii) have at least three years practical experience related to their education field. CPE is not mandatory.

The COAA has also created a local chapter of the US-based Institute of Internal Auditors (IIA). More recently, the nongovernment, not-for-

profit Association of Certified Accountants of Azerbaijan (ACAAz) was established in 2000. The Association currently has 18 active practitioner members, all of whom have completed training in international accounting standards and practices. Nineteen other specialists are undergoing certification and around 80 others are undertaking courses.

The International Regional Federation of Accountants and Auditors Eurasia is not an Azerbaijan-based professional accountancy body, but influences accountancy developments within the FSU and within Azerbaijan. This Federation was established in 1999—its members include 20 professional accountancy organizations from 10 FSU countries. The Federation’s mission is to develop and strengthen the accounting and audit profession, promote the implementation of international professional standards and professional standards on ethics as developed by IFAC and IASB through its member bodies.

The Federation provides support and assistance to national organizations of accountants and auditors in the following areas: (i) developing national organizations in preparation for IFAC recognition; (ii) ensuring high quality accounting and audit services; (iii) developing the theory and practice of accounting and audit based on international standards; (iv) preserving the professional independence of accountants and auditors; and (v) developing and strengthening professional contacts at the regional and international levels. Azerbaijan is represented on each of the Federation’s five standing committees: accounting standards, auditing standards, legal reform, membership and ethics, and professional education and certification.

The Azeri accountancy profession is in its infancy. Not surprisingly, COAA has noted that fees charged by foreign auditors are around 23 times higher than those charged by domestic auditors. The profession can narrow this gap over time by pushing accountants to higher certification standards.

Accounting and Auditing Standards

In common with most other countries transiting from the Soviet accounting system, Azerbaijan continues to emphasize uniform accounting systems. These comprise sector-specific charts of accounts supported by detailed accounting rules and instructions.

In the 1990s, while government focused on the conflict and on developing the oil and gas sector, accounting reform was accorded a low priority. Moreover, the MOF worked, and continues to work, within tight resource constraints (it has received no external technical assistance to

date for accountancy reform). Consequently, Azerbaijan's transition towards IAS-based accounting standards has generally been slower than other FSU countries.

The *Accounting Law 1995* and the *Banking Law 1996* assign accounting standard-setting responsibilities to the MOF and to the Azerbaijan National Bank (ANB). Neither law explicitly refers to IAS. Furthermore, the oil production sharing agreements exempt relevant foreign companies from following Azerbaijan accounting standards; most of these companies use IAS.

Substantial progress has been made towards implementing IAS-based financial reporting in the banking sector. The MOF recently presented an *Accounting Reform Plan* to the Cabinet of Ministers for consideration and approval. The draft plan reflects objectives that are largely inconsistent with accounting in a market economy. For instance, a primary purpose of financial accounting is considered to be the provision of information, in a standard format, that is needed to prepare consolidated country financial statements, which incorporate all entities, both private and public sector. The plan also emphasizes the continued development of UASs.

COAA promulgates auditing instructions in accordance with regulations issued under the *Auditing Services Law 1995*. These instructions are directly based on ISAs. The development process is consultative. Once approved by the COAA Board, auditing standards are registered with the Ministry of Justice. As of December 2001, the Chamber had reviewed, amended and promulgated about 24 of the 30 ISAs.

Education and Training

Together with other FSU states, Azerbaijan has a high literacy rate and comparatively high educational standards. Indeed, Azerbaijan education was renowned within the Soviet Union and more widely (particularly education related to the oil and gas sectors).

However today, most higher education institutions suffer from resource constraints and infrastructures have deteriorated considerably. Moreover, post-independence difficulties have constrained the development of quality academic materials including textbooks. Furthermore, computer hardware and software are lacking and high Internet fees exclude most academics and students from accessing web-based information resources.

One state institution—the State University of Economics—offers undergraduate and postgraduate accountancy programs. As of November

2001, 1,100 students were enrolled in its accountancy-based bachelor programs and 90 were undertaking masters programs. The state specialist schools, for instance the Oil and Gas Academy, also teach specialist accountancy studies.

Eight private tertiary institutions offer accountancy programs, two of these teach predominantly in English. Furthermore, practical accountancy training is given by 26 vocational schools and the newly-established Azerbaijan Banking Training Center provides specialist education in banking and finance. The ACAAz, the Azerbaijan Association of Entrepreneurs and COAA also conduct accounting and auditing training.

The quality of higher education is constrained by ad hoc curriculum development and a general absence of continuing education for accountancy lecturers and professors—the latter is critical in the dynamic environment of transitional Azerbaijan. The move towards the Azeri language further exacerbates problems. For accountancy in particular, there is a chronic lack of textbooks and other teaching materials. Moreover, those that are available are either outdated or unsuitable in the Azeri context.

Government Budgeting and Accounting

Although government finances are in deficit, projected revenues from the oil and gas sector make the current situation sustainable. Indeed government has established a significant Oil Fund and has indicated a medium-term intention to substantially reduce reliance on external assistance. The Oil Fund will support the competitiveness of the non-oil sectors and contribute to intergenerational fiscal stabilization.

However, public sector management arrangements have been characterized as inefficient, ineffective and nontransparent. In the past two years, the Government has prioritized public expenditure management reforms. These include: (i) the ongoing development of a Medium-Term Expenditure Framework (MTEF) for use in budget preparation. Future budget submissions will provide reference to the MTEF, as well as detailed information on expenditure classifications, contingent liabilities, extra-budgetary activities, and the consolidated and general government budgets outturns for the previous year; (ii) drafting amendments to the *Budget Systems Law* and revisions to budget regulations; (iii) beginning in 2001, the publication of quarterly reports on the consolidated government budget execution, including revenues, expenditures, expenditure arrears, stock of government and government-guaranteed debts, and new loans contracted or loan guarantees issued prepared by the MOF; (iv) integration of extra-

budgetary activities into the state budget beginning with the 2002 budget; and (v) strengthening the MOF internal audit function.

Government activities are generally accounted for on an accrual accounting basis at the organizational level and on a cash basis for consolidated budgeting and reporting—the cash basis was introduced with support from international institutions, particularly the IMF and the World Bank.

Government organizations prepare monthly cash reports and quarterly accrual reports that are submitted to the MOF. In 2001, the MOF began publishing consolidated quarterly reports incorporating revenues, expenditures, expenditure arrears, stock of government and government-guaranteed debts, and new loans contracted or loan guarantees issued. A revised *Budget Systems Law* has been drafted and is currently being considered.

Although government organizations are staffed with ‘accountants’ and bookkeepers, these personnel have received little ongoing training. Moreover, concerns over the suitability of their qualifications have been raised, given the changed economic environment and the transition from the centrally-planned to the market economy.

Donor Assistance

Government has announced its intention to significantly reduce its reliance on external assistance within five years. Azerbaijan joined ADB in December 1999. Although no active or planned loan projects are directly related to improving financial governance arrangements, Technical Assistance (TA) No. 3661: *Capacity Building for Strategic Economic Policy Formulation in the Ministry of Finance* (\$0.762 million: 2001-2002) includes: (i) assisting the development of a Macroeconomic Policy Group (MPG); (ii) providing strategic policy advice on structural reform and macroeconomic policy; (iii) improving the information base for MOF economic policy development; (iv) enhancing MOF forecasting and program design capacity and improving fiscal analysis; and (v) developing a macroeconomic framework and public investment program criteria in coordination with MPG and the MOF’s Debt Management Department, and strengthening the Project Evaluation Unit.

The European Bank for Reconstruction and Development (EBRD) emphasizes programs and activities that support privatization, financial reforms, industrial restructuring, the creation and strengthening of infrastructure, foreign investment inflows and environmental rehabilitation. EBRD also provides assistance to organizations to improve their accounting and financial reporting capabilities. Furthermore, EBRD

is currently considering providing assistance to the State Securities Committee to align securities laws and regulations with international practices. The IMF has provided assistance to improve macroeconomic policies and to strengthen central bank functions.

The **World Bank** is the key player in supporting improved financial governance arrangements. In addition to strengthening executing agency accounting arrangements and financing external financial audits, the following projects are relevant:

- Pipeline: *Institution Building Technical Assistance Project II* (\$16.0 million: 2002–). This project has two components: Public Sector Reform (PSR) and Financial Sector Reform (FSR). The PSR component is intended to: (i) improve public resource management; (ii) strengthen the accountability, efficiency and policy implementation capacity of the central government; (iii) improve public service delivery; and (iv) develop the legal system and an independent judiciary. The FSR component will focus on: (i) assisting the Government to privatize state banks; (ii) assisting the ANB to strengthen banking supervision; and (iii) strengthening the legal and regulatory environment.
- Project P055131: *Second Structural Adjustment Credit Project* (\$60.0 million: 2002–). This project will support the Government’s public sector reforms. In doing so, it is intended to contribute to improved public financial management, including: (i) better management of public resources—human, financial and natural; (ii) improved delivery of public services; and (iii) an enabling environment for private sector development
- Loan 35180: *Financial Sector Technical Assistance Loan Project* (\$5.4 million: 2001–2006). This project supports implementation of the Government’s financial sector development strategy, including: (i) introducing IAS-based National Accounting Standards for commercial banks; (ii) establishing IAS-compatible National Accounting Standards; (iii) passing laws and regulations to reinforce these National Accounting Standards; (iv) developing commercial bank financial reporting based on ANB-prescribed standards, and (v) preparing a banking manual of procedures and guidelines for accounting practices.
- Loan 27690: *Institution Building Technical Assistance Project* (\$18.0 million: 1995–2001). This project had four focal areas: (i) assisting privatization and enterprise reform; (ii) strengthening macroeconomic management; (iii) developing the financial sector; and (iv) providing legal technical assistance. Among other things, the assistance supported

the development of accounting and auditing systems and standards for enterprises and banks, and the implementation of a computerized accounting system within ANB.

European Union—Technical Assistance to the Commonwealth of Independent States (EU-TACIS) assistance includes: supporting institutional, legal and administrative reforms; and supporting the private sector and assisting economic development. Particular attention is focusing on developing internationally-acceptably accounting standards. The United States Agency for International Development (USAID) is providing assistance to support the introduction of IAS and to develop qualified financial experts in order to facilitate a countrywide transfer to international standards of financial reporting (through assistance to the ACAAz).

Issues and Recommendations

This Diagnostic Study of Accounting and Auditing identifies issues and recommendations that are associated with gaps or weaknesses in Azerbaijan's accounting and auditing arrangements. These recommendations are intended to supplement and support existing strategies and projects. Where actions are already planned or underway—for instance, upgrading information systems—no recommendations are made. Issues are separated into: (i) those that are able to be resolved without the need for external assistance; and (ii) those that are better able to be resolved with external assistance.

The study concludes that—with some exceptions—much remains to be done to align Azerbaijan accounting and auditing arrangements with international practices and with the needs of the mixed market economy. These changes include developing a supportive and appropriate legislative and institutional environment, reforming accounting standards and strengthening the accounting and auditing profession. Internationally-compatible arrangements can only be successfully implemented with the support of a strong profession comprising skilled accountancy professionals.

Azerbaijan is now in a position to closely examine other countries' efforts and—by doing so—to develop a comprehensive road map for accountancy reform that (hopefully) will enable it to avoid the errors made by other countries. To this end, this DSAA recommends that a coordination group be established to: (i) develop a strategic plan for accountancy reform; and (ii) design and agree a legislative and institutional framework that will support implementation of the strategic plan.

I. Introduction

1. Study Background

The 1997-1998 Asian financial crisis exposed structural weaknesses in the banking and corporate sectors of affected countries owing largely to poor governance, a lack of transparency, and weak supervision and regulation.³

Asian Development Bank (ADB) has been taking a number of initiatives to assist Developing Member Countries (DMCs) to overcome these structural problems. The focus on improved governance includes enhancing the effectiveness of public administration and development management at the sector level and in national institutions. Where appropriate, institutional development of the local and provincial agencies and the private sector is also covered. A sound regulatory financial framework and its enforcement, capable institutions, skilled human resources, and effective monitoring and supervision are important prerequisites to an efficient financial structure.

In 2000, under ADB Regional Technical Assistance (RETA) 5877⁴, Diagnostic Studies of Accounting and Auditing (DSAAs) were prepared and published for Cambodia, Mongolia, Pakistan, Papua New Guinea, People's Republic of China, Uzbekistan and Viet Nam. ADB approved RETA 5980—*Diagnostic Study of Accounting and Auditing Practices in Selected DMCs*⁵—for the purpose of carrying out initial studies to identify gaps and weaknesses in accounting and auditing arrangements and to recommend courses of action to overcome these problems. It extends the work conducted under RETA 5877.

2. Objectives

ADB has demonstrated its stand on the importance of good governance, through effective financial management, for sustained economic development. This RETA involved a diagnostic review of the existing accounting and auditing support and standards available in the selected

³ Zhuang, Juzhong, David Edwards, David Webb and Ma. Virginita Capulong. 2000. *Corporate Governance and Finance in East Asia: A Study of Indonesia, Republic of Korea, Malaysia, Philippines and Thailand*. Manila: ADB.

⁴ *Strengthening Financial Management and Governance in Selected DMCs*.

⁵ For \$230,000 approved on 20 March 2001.

DMCs. After carrying out this diagnostic review, the study assessed the need for assistance to improve the current situation. Objectives were to:

- (i) assess the capability and capacity within each country to provide efficient and effective accounting and auditing support to meet international standards and best practices and address the issue of training and capacity enhancement
- (ii) determine the existing accounting and auditing standards of each selected country
- (iii) assess the degree of deviation from International Accounting and Auditing Standards while identifying weaknesses and possible corrective options
- (iv) discuss the fieldwork findings and introduce the concepts of the international standards through workshops, and
- (v) determine the level and type of assistance needed by each country in order to provide acceptable accounting and auditing support to the private and public sectors.

3. Scope

The RETA involved an indepth study of the key issues relating to accounting and auditing support in the selected DMCs, identified gaps and weaknesses that need to be addressed to improve accounting and auditing support, and developed assistance programs in collaboration with other donors to rectify the identified weaknesses. Azerbaijan was one of four countries that participated in the RETA.

4. Country Case Studies and Workshop

The first part of the study examined the current accounting and auditing structure and systems adopted in Azerbaijan. It also: (i) analyzed the political, institutional, and regulatory and legal framework on accounting and auditing practice and the level of enforcement of existing laws, rules, and regulations; (ii) identified gaps and weaknesses in accounting and auditing support available and deviations from international standards; and (iii) identified alternative options to remedy the identified weaknesses, with the objective of eventually doing away with these.

The second part of this study disseminated the country-research findings through in-country workshops. Each workshop provided a cross-section of views on the research findings and established ways to move forward to improve financial management and governance in the country.

After carrying out the assessment of accounting and auditing support in Azerbaijan, the study findings and recommendations were discussed at a workshop in Baku on 5-6 December 2001, and at an international workshop at ADB Headquarters in Manila from 5-6 March 2002. This report incorporates feedback from both workshops. Appendix 3 provides further information on the study process and the Baku workshop.

5. Azerbaijan

General

The Caucasus Mountains form a geological, cultural and political boundary between Asia and Europe. Azerbaijan, Armenia and Georgia comprise the South Caucasus region, which is sandwiched between the Black and Caspian Seas to the West and East, and bordered by Russia to the north, and Turkey and Iran to the south.

Azerbaijan is the largest and most populous of the South Caucasus countries—recent estimates indicate a population of approximately 8 million of whom a quarter live in the capital Baku. This population comprises different ethnic groups, including Azeris (90 percent), Dagestanis (3.2 percent) and Russians (2.5 percent).

In the 19th century, Azerbaijan—then part of the Russian empire—experienced an unprecedented oil boom, which attracted international investment. By the beginning of the 20th century, it was supplying almost half of the world's oil. After a brief period of independence, Azerbaijan became a socialist republic within the Soviet Union in 1922.

The oil-rich country gained independence from the Soviet Union in 1991 amid war and political turmoil. A 1994 ceasefire ended an armed conflict with Armenia. However, about one seventh of Azerbaijan's territory remains occupied, while around 800,000 refugees and internally-displaced persons (IDPs) are scattered around the country.

Azerbaijan is a presidential republic. The President and the Parliament (*Milli Mejlis*, which has 125 members) are elected every five years. The national language is Azeri, spoken by 89 percent of the population. Most people also speak Russian. In addition to oil and gas reserves, Azerbaijan's assets include a well-educated population. However, almost 70 percent of the population lives below the poverty line (i.e., less than a dollar a day)—the worst affected are the refugees and internally-displaced persons. Major exports include oil and gas (70 percent), machinery, cotton and foodstuffs. Major imports are machinery and equipment, metals and chemicals. Table

It presents key indicators for Azerbaijan and for other selected countries.

In 1994 Azerbaijan signed a 30-year contract worth \$7.4 billion with a British Petroleum-led consortium. A number of production-sharing arrangements (PSAs) have since been negotiated with foreign firms, which have thus far committed \$60 billion to oil and gas field development. Production under the first PSA began in November 1997.

Table 1: Key Indicators for Selected ADB DMCs^{6, 7}

| Indicator | Azer- bajjan | Fiji Islands | RMI | Philip- pines | Sri Lanka |
|---|-----------------|-----------------|---------|------------------|--------------|
| General | | | | | |
| Population (<i>thousands, 2000</i>) | 8,049.0 | 811.0 | 51.6 | 78,400.0 | 19,359.0 |
| Population density (<i>people per km², 2000</i>) | 93.0 | 44.0 | 282.0 | 263.0 | 295.0 |
| Urban population (<i>% of total, 2000</i>) | 57.3 | 42.3 | 71.9 | 58.6 | 23.6 |
| Average annual pop. growth rate (<i>%, 1995-2000</i>) | 1.0 | 1.1 | 1.5 | 2.2 | 1.3 |
| Social | | | | | |
| Under-five mortality rate (<i>per 1000, 1999</i>) | 16.0 | 18.0 | 63.0 | 31.0 | 15.0 |
| Life expectancy at birth (<i>years, 1999</i>) | 71.0 | 67.0 | 65.0 | 69.0 | 74.0 |
| Adult literacy rate (<i>15-yr+, %, 1999</i>): | | | | | |
| – Females | 96.0 | 90.0 | 97.0 | 95.0 | 89.0 |
| – Males | 99.0 | 95.0 | 97.0 | 95.0 | 94.0 |
| Population in poverty (<i>%, 1995-99</i>) | 68.1 | 25.5 | ... | 40.0 | 26.7 |
| Human Development Index (<i>1999</i>) | 0.74 | 0.76 | 0.56 | 0.75 | 0.74 |
| Economic | | | | | |
| Gross National Product (<i>\$ million, 1999</i>) | 3,705.0 | 1,848.0 | 99.0 | 77,967.0 | 15,578.0 |
| GDP per capita (<i>\$, 2000</i>) | 654.0 | 1,978.0 | 1,890.0 | 959.0 | 842.0 |
| GDP growth rate (<i>%</i>) | | | | | |
| – 2000 | 11.4 | -9.3 | -2.3 | 4.0 | 6.0 |
| – 1999 | 7.4 | 9.6 | 0.8 | 3.4 | 4.3 |
| – 1998 | 10.6 | 1.4 | -16.0 | -0.6 | 4.7 |
| – 1997 | 8.8 | -0.9 | -9.4 | 5.2 | 6.3 |
| Consumer Price Index (<i>Annual % change, 2000</i>) | 1.9 | 1.1 | -1.9 | 4.4 | 6.2 |
| Fiscal Balance / GDP (<i>%, 2000</i>) | -1.0 | ... | -35.5 | -4.2 | -9.9 |
| Total External Debt / GNP (<i>%, 1999</i>) | 30.0 | 9.3 | ... | 64.8 | 60.3 |

⁶ Asian Development Bank (ADB). 2001. *Key Indicators of Developing Asian and Pacific Countries*. Volume XXXII. Manila: ADB.

⁷ Asian Development Bank (ADB). 2001. *Asian Development Outlook 2001*. Manila: ADB. pp. 139-140.

Table 1: Key Indicators for Selected ADB DMCs (*continued*)

| Indicator | Azer- bajjan | Fiji Islands | RMI | Philip- pines | Sri Lanka |
|-----------------------------------|-----------------|-----------------|---------|------------------|--------------|
| Official Development Flows | | | | | |
| US\$ million (1999) | 207.2 | 23.2 | 62.9 | 295.0 | 343.6 |
| Dollars per capita (1999) | 25.7 | 28.6 | 1,219.0 | 3.8 | 17.7 |
| Percentage of GNP (1999) | 5.6 | 1.3 | 63.5 | 0.4 | 2.2 |

Recent Economic Trends⁸

Azerbaijan shares all the transition problems of other Former Soviet Union (FSU) countries. Due to the unstable domestic situation, it embarked on economic reforms later than most other FSU countries. Since the mid-1990s Azerbaijan has made progress on establishing a market economy and restoring macroeconomic stability. A privatization program was introduced in September 1996—within three years, over 21,000 small enterprises had passed into private hands. Inflation of 1,500 percent in 1994 declined to 160 percent in 1995 and to just six percent in 1996.

Economic performance was strong in 2000, with real GDP growth accelerating to 11.4 percent from 7.4 percent in 1999. The major contributing factor was the 20-plus percent upsurge in the oil and oil-related sectors in the first half of 2000, which benefited from rising world oil prices. In contrast, the agriculture sector grew by just 6 percent. Growth in other labor-intensive sectors was also weak. Consequently, unemployment was estimated at 18 percent in 2000.

Government adopted a tight fiscal stance in 2000 and reduced the fiscal deficit to 2.3 percent of GDP in 2000, from 5.4 percent in 1999. Improved budget revenues and lower levels of public expenditures contributed to a fiscal surplus in the first quarter of 2001 (1.1 percent of GDP).

Estimates are that GDP grew by 9.9 percent in 2001; largely due to oil sector development and improved agricultural performance.

Financial Governance: Issues and Challenges

The unresolved conflict impedes economic progress and deters foreign investment. Long-term prospects depend upon world oil prices, the

⁸ Primary Source: Asian Development Bank (ADB). 2001. *Asian Development Outlook 2001*. Manila: ADB.

location of new regional pipelines and Azerbaijan's ability to manage its oil wealth. Maintaining the competitiveness of non-oil exports in world markets is also a serious long-term challenge.

The Government has initiated structural reforms and has substantially liberalized domestic markets and foreign trade. Another government priority is the recently rejuvenated privatization program for medium- and large-scale organizations—the privatization law was passed by parliament in 2000.

The Government established the State Oil Fund in November 1999 (an intergenerational trust fund, similar to those established by several Pacific island nations). The Fund will enable better management of oil revenues. In addition, progress has been made in implementing policy reforms, such as the passage of the *Civil Code* (effective 1 September 2000) and the amended *Tax Code* (effective 1 January 2001). However, structural reforms, particularly in the banking sector, have lagged behind. Crucial reforms are needed in this sector to improve supervision and strengthen enforcement of prudential regulations in line with international best practice.

The amended *Tax Code 2000* is expected to increase fiscal revenues. However, increasing social expenditures while maintaining fiscal discipline remains a challenge, as does managing projected oil revenues and developing the non-oil sectors.

To maintain investor confidence, the Government needs to make a serious effort in implementing structural reforms. Important areas include privatization, financial sector restructuring, and good governance to establish institutions and the rule of law conducive to a market-based economy. The increasing dependence on oil exports is a concern—developing the non-oil sectors is critical to achieving a balanced external account position and sustainable growth. Understanding this, the Government has prioritized non-oil sector advancement in its recent medium-term development strategy.

The principal elements of the medium-term development strategy include: (i) maintaining fiscal and monetary policies that support macroeconomic stability; (ii) implementing aggressive programs to strengthen energy sector governance and financial discipline; (iii) maintaining the liberal trade regime; (iv) accelerating structural reforms; and (v) implementing measures that will improve the legal and regulatory environment for private sector development.

As part of the government's overall effort to enhance governance, a comprehensive anticorruption program is being developed and the Azerbaijan Accounting Chamber (AAC)—Azerbaijan's Supreme Audit

Institution (SAI)—has been established. The AAC has the authority to audit all government bodies, including all budgetary and extra-budgetary organizations and funds, and must publicly report its findings.⁹

6. ADB Operational Strategy

ADB's interim operational strategy for Azerbaijan focuses on reducing poverty and raising living standards in a sustainable manner. Operations will initially: (i) enhance human development; (ii) promote sustainable growth, including private sector development; and (iii) support good governance and institutional strengthening. Two operational areas are prioritized: direct assistance to the poor, and poverty reduction through non-oil sector development.¹⁰

7. International Guidelines and Surveillance¹¹

The international community is supporting the development of guidelines, standards, and codes to assess financial management and governance practices (see Table 2). Where relevant, this report compares Azeri arrangements and practices against these benchmarks.

These guidelines, standards and codes—to varying extents—all involve accounting and auditing arrangements. Furthermore, in an attempt to identify and avoid potential crises before they occur, the IMF and the World Bank have together embarked on a series of *Reports on the Observance of Standards and Codes (ROSCs)*. These reports summarize the extent to which countries observe certain internationally recognized standards.¹² Although ROSCs are intended to be voluntary, the information provided by each country (or not provided, as the case may be) is likely to influence country dealings with International Financial Institutions, and the level of

⁹ International Monetary Fund (IMF). 15 June 2001. *Azerbaijan Republic: Memorandum of Economic and Financial Policies for 2001-02*. Washington DC: IMF. URL: <http://www.imf.org/external/np/loi/2001/aze/01/index.htm>

¹⁰ Asian Development Bank (ADB). 2001. *Regional and Country Highlights: Azerbaijan*. Manila: ADB. p 14.

¹¹ Narayan, Francis B., Ted Godden, Barry Reid, and Maria Rosa Ortega. 2000. *Financial Management and Governance Issues in Selected Developing Member Countries: A Study of Cambodia, People's Republic of China, Mongolia, Pakistan, Papua New Guinea, Uzbekistan, and Viet Nam*. Manila: ADB. pp. 12-13.

¹² International Monetary Fund (IMF). September 2000. *Experimental Reports on Observance of Standards and Codes (ROSCs)*. Washington, DC: IMF. URL: www.imf.org/external/np/rosoc

confidence that investors and the international financial community have in a country.

Table 2: Selected International Guidelines, Standards and Codes

| International Guideline, Standard or Code | Promulgated By |
|--|---|
| • Principles of Corporate Governance | Organisation for Economic Cooperation and Development (OECD) |
| • Code of Good Practices on Fiscal Transparency | International Monetary Fund (IMF) |
| • Code of Good Practices on Transparency of Monetary and Financial Policies | International Monetary Fund (IMF) |
| • Implementation of the Objectives and Principles for Securities Regulation assessment surveys | International Organization of Securities Commissions' (IOSCO) |
| • International Accounting Standards (IASs) | International Accounting Standards Board (IASB) |
| • International Standards on Auditing (ISAs) | International Federation of Accountants (IFAC) |
| • Draft Banking Supervision Guidelines | Basel Committee on Banking Supervision (BCSB) of the Bank for International Settlements (BIS) |

8. Report Structure

This report examines financial management and governance issues in Azerbaijan, with a focus on accounting and auditing arrangements. In addition to this introduction, the report has the following chapters:

- Chapter II—**Accounting and Auditing in Azerbaijan**—presents an overview of Azeri accounting and auditing arrangements. It provides context for the following chapters on professional infrastructure, accounting and auditing standards, accounting and auditing training, and government budgeting and accounting arrangements.
- Chapter III—**Professional Infrastructure**—describes Azerbaijan's professional accountancy infrastructure.
- Chapter IV—**Accounting and Auditing Standards**—describes the accounting and auditing standards that govern the preparation of external financial reports and the audit of those reports.

- Chapter V—**Accounting and Auditing Training**—describes accounting and auditing education and training, including coordination of accountancy education.
- Chapter VI—**Government Budgeting and Accounting**—describes government budgeting and accounting arrangements.
- Chapter VII—**Donor Assistance**—reviews donor coordination mechanisms and discusses donor activities in relation to financial management and governance arrangements.
- Chapter VIII—**Issues and Recommendations**—presents the issues and recommendations that are associated with gaps or weaknesses in accounting and auditing arrangements.
- Chapter IX—**Country Action Plan**—summarizes deficiencies and actions to address these deficiencies. Recommendations are divided into actions that would be better achieved with external assistance; and actions that may be achieved without the need for external assistance.

II. Accounting and Auditing in Azerbaijan

This chapter presents an overview of Azerbaijan accounting and auditing arrangements. It provides context for the following chapters on professional infrastructure, accounting and auditing standards, accounting and auditing training, and government budgeting and accounting arrangements. The chapter comprises eight sections as follows:

Part One: Accounting

- 1 – Introduction—identifies historical factors that have influenced accounting arrangements.
- 2 – Issues and Responses since 1991—describes the issues that faced Azerbaijan in 1991 when the transition process to a market economy began. It also summarizes the actions that were taken in response to these issues.
- 3 – The ‘Azerbaijan Accounting System’—describes Azerbaijan accounting arrangements, which include the legislative and institutional framework, financial reporting requirements, accounting bases, accounting information systems and record-keeping arrangements.

Part Two: Auditing

- 4 – Introduction—introduces Azerbaijan auditing arrangements.
- 5 – Governing Laws and Regulations—describes the laws that govern Azerbaijan auditing practices and audit requirements.
- 6 – Public Sector Auditing: The Azerbaijan Accounting Chamber (AAC)—briefly describes the establishment of the AAC, Azerbaijan’s Supreme Audit Institution (SAI).
- 7 – Accounting and Auditing Firms—describes the presence of domestic and international accounting firms in Azerbaijan.
- 8 – Issue Synopsis: Azerbaijan Accounting and Auditing—summarizes the issues identified in this chapter.

Part One. Accounting

1. Introduction

Accounting in the Soviet Union, which included Azerbaijan, catered to the needs of statistical and tax authorities. It did not provide the information required by securities markets or company managers in a market economy. Nor did it support an economically rational system of enterprise taxation, since many production costs were not deductible for tax purposes (e.g., certain payroll and interest expenses).

In common with other former Soviet Union (FSU) countries, Azerbaijan has little history or tradition of using market-based accounting concepts such as going concern, consistency and substance over form. In particular, the Soviet accounting system strictly applied the historical cost convention to record assets—assets that were never revalued. Moreover, provisions for doubtful debts or obsolete inventories were not estimated—doubtful accounts were written off only when they were clearly not collectable. In essence, a risk-free environment was assumed where no thought need be given to valuation of assets or determination of profit. Goods were not bought and sold in a free market and there was no risk of a decline in value. Enterprises did not answer to investors, bankers or regulators for their performance.

Accounting consisted of adhering to prescribed charts of accounts (Uniform Accounting Systems: UASs) that were designed to meet the requirements of the central planning system. The primary function of accounting was to record the factual data necessary to assess plan accomplishments, rather than to assess an enterprise's financial situation. The focus of Soviet accounting was more on bookkeeping than on the process of accounting. In fact, they were considered the same thing. Accounting, however, involves much more than bookkeeping. Bookkeeping only entails the recording of economic events while the accounting process includes application of generally accepted accounting standards to identify, measure, record and report those events and their effect on an enterprise.

Upon independence in 1991, Azerbaijan found itself in the same position as other Former Soviet Union (FSU) countries concerning accounting arrangements. However, the Soviet accounting system created a sound basis on which to build—the system used many concepts of modern accounting including accrual measurement and double entry bookkeeping. Moreover, large numbers of bookkeepers were trained in these concepts and were proficient in their application.

2. Issues and Responses since 1991

In the decade since the beginning of the transition, Azerbaijan has made some progress in developing an accounting infrastructure suitable to the needs of a market economy. However, financial management reforms were slow-tracked due to emphasis on the conflict and oil and gas sector developments. Consequently, Azerbaijan's accounting and auditing reforms lag those of many other FSU countries.

However, the magnitude of these accomplishments is best viewed by examining the 1991 situation. First, although there were tens of thousands of bookkeepers, there were no qualified Certified Practising Accountants (CPAs) let alone a professional accounting body. Second, financial information on the performance and position of organizations was not publicly available. In any case, this information did not meet international standards nor did it cater to the needs of investors or lenders. Third, the users of financial information (investors and creditors) were unfamiliar with what they should demand from organizations. Fourth, financial information was not independently verified (audited) to international standards and could not be relied upon. Fifth, the entire legal framework was geared to central planning and specified exactly what information should be produced, how it should be produced, and to whom it should be provided. Finally, the regulatory entities that generally exist in market economies to oversee financial disclosure practices, such as securities exchange commissions, did not exist.

At the beginning of the transition, many FSU accountants believed that transforming accounting to a market-oriented system could be accomplished simply by modernizing the UASs (charts of accounts, supported by detailed instructions) according to internationally accepted accounting principles. However, this was not sufficient—international accounting standards (IASs) and practices must be underpinned by the exercise of professional judgment—the development of a strong accountancy profession whose members are equipped to understand the conceptual underpinnings of IAS, and who are able to exercise judgment in their application, is now seen as critical to the effective establishment of international accounting standards and practices.

The adoption of the *Accounting Law 1995* and the 1996 introduction of new UASs brought the Azerbaijan accounting system closer to IASs. In particular, (i) market-based accounting concepts were introduced (e.g., leasing); (ii) enterprises were allowed some freedom over asset accounting; (iii) enterprises may now provide for doubtful debts; and (iv) financial statement formats were revised.

3. The ‘Azerbaijan Accounting System’

Legislative and Institutional Framework

Articles 120–125 of the *Civil Code 1999* govern accounting and auditing arrangements in Azerbaijan. In particular, the *Civil Code 1999* stipulates the structure of financial statements. The Ministry of Finance (MOF) administers the *Law on Accounting 1995*, which regulates the maintenance of accounting records and the preparation of balance sheets by business entities and organizations in both the private and the public sectors. It also sets out financial reporting requirements.

Other relevant laws include the *Joint Stock Companies Law 1994* (Appendix 16), the *Enterprises Law 1994* (see Appendix 15), the *Banking Law 1996* (see Appendix 14) and the *Tax Code 2000*. These laws conflict in places regarding accounting and reporting arrangements. At the same time, the prescriptive nature of the *Civil Code 1999* conflicts with the flexible provisions of the *Tax Code 2000*.

The main reporting requirements for legal entities are the quarterly tax return and statutory accounting annual reports that are filed in March–April. The accounting arrangements for relevant foreign companies usually exempt these companies from following Azerbaijan accounting practices.

Accounting and reporting arrangements in the banking sector have developed further than those of other sectors. The MOF has recently prepared a five-year *Accounting Reform Plan* to develop accounting arrangements for other sectors (see Appendix 4, Appendix 5 and Appendix 6). This plan is currently being considered and covers accounting standards, certification, ethics and training.

Accounting Bases and Principles

Revenues can be recorded on either the cash or accrual basis. Expenses must be recognized on the accrual basis, except where the cash basis has been used for revenues, in which case direct costs must be recorded on the cash basis (*Tax Code 2000*, Articles 130–134). Budgetary organizations use the accrual accounting basis.

Accounting Information Systems

The books of many organizations and enterprises are maintained manually. However, computerized accounting information systems are becoming

prevalent, particularly in the oil and gas, and in the banking sector. The IMF and World Bank are supporting the development of computerization of government accounting. Furthermore, it appears that the *Accounting Reform Plan* (See Appendix 5) envisages a national computerized accounting system.

Record-Keeping Arrangements

With the exception of organizations operating under Production Sharing Agreements (PSAs), all entities established under Azerbaijan laws must maintain their books and records in Azeri, in local currency, and in accordance with accounting legislation. This includes using the appropriate UAS.

Part Two. Auditing

4. Introduction

Up until 1991, auditing in the Soviet Union, which included Azerbaijan, reflected the highly prescriptive nature of the underlying accounting system. It was primarily a verification exercise, with the final accounts being compared to bookkeeping records by accountants from another enterprise within the same group. It is not surprising that a fully functioning and competent audit profession has not been created within the short timeframe of 10 years. With the exception of a few large international firms, auditing in accordance with International Standards on Auditing (ISAs) is a relatively new concept.

5. Governing Laws and Regulations

The *Auditing Services Law 1995* governs auditing activities in Azerbaijan. Other laws stipulate audit requirements. In general, all organizations must be audited. The *Auditing Law 1995* describes the ‘Audit Conclusion’ as an estimation of an organization’s financial state.

6. Public Sector Auditing: The Azerbaijan Accounting Chamber (AAC)

The Government has recently moved to establish a Supreme Audit Institution (SAI)—the Azerbaijan Accounting Chamber (AAC). The AAC

will have the authority to audit all government bodies, including all budgetary and extra-budgetary organizations and funds, and will be obligated publicly report its findings. The AAC Chair was appointed at the end of 2001. The Chamber is currently in the process of hiring staff, developing capacity and preparing a work program.

7. Accounting and Auditing Firms

As of April 2001, the Chamber of Auditors of Azerbaijan (COAA) had issued audit licenses to 27 local firms and five foreign firms. Four of the ‘Big Five’ international accounting firms have offices in Azerbaijan: PricewaterhouseCoopers, Ernst & Young, Arthur Andersen and KPMG. Deloitte Touche Tohmatsu maintains a presence through an associated firm. The five licensed foreign accountancy firms earned 78 percent of total fees during the first half of 2001—their fee structures are about 23 times higher than domestic counterparts.¹³

8. Issue Synopsis: Azerbaijan Accounting and Auditing Arrangements

Chapter IX—*Issues and Recommendations*—identifies and describes constraints and proposes corrective actions. These include the following issues from this chapter:

- With exceptions—particularly in the banking and the oil and gas sectors—Azerbaijan’s accounting and auditing arrangements remain largely consistent with the Soviet accounting arrangements.
- In some places where reforms have been made, conflicts have been created between laws and regulations.
- To this end, the MOF has prepared an *Accounting Reform Plan*—the Cabinet of Ministers is currently considering the plan.

¹³ *Azeri Business News*. 2001 August 29. Interview with the Chairman of Chamber of Auditors of Azerbaijan. Newspaper Article.

III. Professional Infrastructure

This chapter describes Azerbaijan’s nascent professional accountancy infrastructure. It is structured as follows:

- 1 – Introduction—provides an overview of Azerbaijan’s accountancy profession.
- 2 – Chamber of Auditors of Azerbaijan (COAA)—describes the legal status and activities of the COAA—Azerbaijan’s national professional accountancy body.
- 3 – Azerbaijan Audit Licenses—identifies the requirements for attaining an audit license.
- 4 – Association of Certified Accountants of Azerbaijan (ACAAz)—describes the establishment and objectives of the ACAAz.
- 5 – Institute of Internal Auditors (IIA)—discusses the establishment of the Azerbaijan chapter of the US-based IIA.
- 6 – IRFAA Eurasia—describes the objectives and activities of the International Regional Federation of Accountants and Auditors Eurasia (IRFAA Eurasia).
- 7 – Issue Synopsis: Professional Infrastructure—summarizes the issues identified in this chapter.

1. Introduction

The Soviet accounting system required neither professional accountants nor an accountancy profession—in the western sense. This changed with Azerbaijan’s transition to a market economy, following independence in 1991.

However, it wasn’t until 1996 that the Chamber of Auditors of Azerbaijan (COAA) was established in accordance with the *Auditing Services Law 1995*. By mid-2001, the Chamber had issued licenses to 160 individuals and 32 firms. The COAA has also established a local chapter of the US-based Institute of Internal Auditors (IIA).

More recently, the Association of Certified Accountants of Azerbaijan (ACAAz) was formally created as a nongovernment organization in 2000. It currently has 18 active members.

The International Federation of Accountants (IFAC) oversees the professional arrangements and procedures of its member bodies. These

include: (i) membership requirements; (ii) continuing professional education; and (iii) quality control arrangements. Although Azeri professional accountancy bodies have yet to join IFAC, the international standards and guidance regarding professional arrangements that Appendix 7 provides are of relevance.

The Azeri accountancy profession is in its infancy—not surprisingly, the COAA has noted that fees charged by foreign auditors are around 23 times higher than those charged by domestic auditors. The profession can narrow this gap over time by tirelessly pushing accountants to higher certification standards.

2. Chamber of Auditors of Azerbaijan (COAA)

Introduction

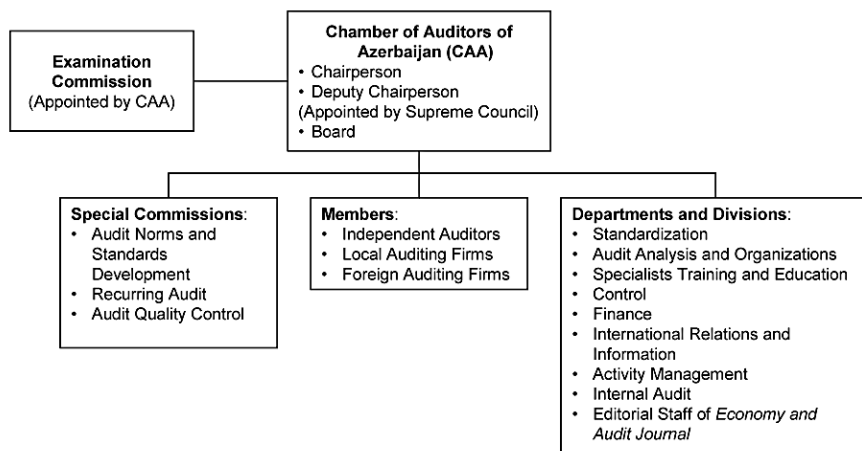
The Chamber began operations in 1996 in accordance with the provisions of the *Auditing Services Law 1995* (see Appendix 12 and Appendix 13). Under these provisions, it is responsible for: (i) overseeing auditing activities in Azerbaijan; (ii) issuing auditing instructions, standards and guidance; (iii) licensing individual auditors and auditing firms; (iv) considering complaints against individuals and auditing firms; (v) consulting the profession on relevant legislative issues; and (vi) reviewing the compliance of foreign individuals and foreign audit firms with the *Auditing Services Law 1995*.

The Supreme Council of the Azerbaijan Republic appoints the Chamber's Chairperson and Deputy Chairperson. Individual auditors and auditing firms are required to pay membership fees to the Chamber. Moreover, they are required to provide statistical information (for instance, fee income), which the Chamber summarizes and provides to tax and statistical bodies. Until January 2001, the Chamber conducted fee-paying audits on its own behalf, and in competition with auditing firms.

Memberships and Affiliations

COAA is a member of the Asian Organization of Supreme Audit Institutions (ASOSAI), the Council of Heads of CIS Countries of Supreme Financial Control Units, Economic Organization of Supreme Audit Institutions (EOSAI), European Organization of Supreme Audit Institutions (EUROSAI), International Regional Federation of Accountants and Auditors Eurasia (IFRAA Eurasia), and International Organization of Supreme Audit Institutions (INTOSAI).

Figure 1: Structure of the Chamber of Auditors (COAA)



In June 2001, it was announced that these memberships and affiliations would be passed from the COAA to the Azerbaijan Accounting Chamber (AAC).

Licensing

As of April 2001, the Chamber had issued audit licenses to 160 individuals, 27 local firms and five foreign firms.

3. Azerbaijan Audit Licenses

Introduction

COAA issues renewable five-year licenses to individuals and firms. Auditing firms must comprise at least three qualified individuals. Individuals must be Azerbaijan citizens, although the Chamber may accept the qualifications of foreigners, who are licensed to practice in their own countries. These licenses are issued in accordance with the *Auditing Services Law 1995* (see Appendix 12).

Educational Requirement

Auditors must have completed higher education in accounting, finance, economics or law.

Examination

License examinations are prepared and supervised by a COAA-appointed Commission in accordance with the *Auditing Services Law 1995*. The Commission comprises representatives from the COAA (three), MOF, Ministry of Taxation, NBA, academia, and practitioners. Each member must have at least 10 years experience in accounting, finance, economics or law.

Practical Experience Requirement

Licensees must have at least three years practical experience related to their field of education.

Continuing Professional Education (CPE)

There is no CPE requirement.

Table 3: Azerbaijan Accountant Qualifications¹⁴

| Requirement | International | Azerbaijan (COAA licensed auditor) | Sri Lanka (ICASL: Chartered Accountant) | California, US (Certified Public Accountant, CPA) |
|-------------|--|--|---|---|
| Education | Recognized education program (IFAC: IEG 9, Para 26). | ✓ Higher education in accounting, finance, economics or law. | ✓ A range of entry qualifications are accepted—a university degree is not necessarily required. | ✓ Core course comprising 45 semester units of accounting, auditing or business-related subjects (a variety of other qualifications are accepted). |
| Examination | A significant portion of responses must be written (IFAC: IEG 9, Para 44). | ✓ Set by COAA-appointed Commission | ✓ Yes. | ✓ Yes. |

¹⁴ Table adapted from: Favere-Marchesi, Michael. 2000. Audit Quality in ASEAN. *The International Journal of Accounting*. Vol 35(1). pp. 121-149.

Table 3: Azerbaijan Accountant Qualifications (continued)

| Requirement | International | Azerbaijan (COAA licensed auditor) | Sri Lanka (ICASL: Chartered Accountant) | California, US (Certified Public Accountant, CPA) |
|-----------------------------------|--|---|---|--|
| Experience | Minimum of three years practical experience in an appropriate, supervised environment (IFAC: IEG 9, Para 49). | <input checked="" type="checkbox"/> Minimum of three years practical experience in the area in which higher education was received. | <input checked="" type="checkbox"/> At least three years for university degree holders and four years for others. | <input checked="" type="checkbox"/> / <input checked="" type="checkbox"/> Two, three, or four years prescribed experience; depending on education level. |
| Continuing professional education | Annual minimum of 30 hours, or 90 hours over each three-year period, of structured learning activities (IFAC, ISAR). | <input checked="" type="checkbox"/> No mandatory requirement. | <input checked="" type="checkbox"/> Recommended but not mandatory. Follows the practice of ICAEW. | <input checked="" type="checkbox"/> 80 hours for each two-year license renewal period (following first license renewal). |

4. Association of Certified Accountants of Azerbaijan (ACAAz)¹⁵

The Association of Certified Accountants of Azerbaijan (ACAAz) was established in 2000. It is a nongovernment, not-for-profit organization. It has 18 active members practitioners, all of whom have completed training in International accounting standards and practices. Nineteen other specialists are currently undergoing certification and around 80 others are undertaking courses.

The Association’s development is being supported as part of a \$125,000 Eurasia Foundation grant to introduce IASs and to develop qualified Azerbaijan financial experts. The project includes: (i) training specialists and producing printed training materials; (ii) introducing a system of accounting certification; (iii) organizing ongoing courses for accounting certification; and (iv) expanding the ACAAz’s activities into the four regions of Azerbaijan.

¹⁵ Primary source: URL: www.ACAAz.org

5. Institute of Internal Auditors (IIA)

The Azerbaijan Chapter of the International Institute of Internal Auditors (IIA) is a suborganization of the COAA. The US-based IIA is a semi-commercial organization—membership is open to individuals. The IIA administers the International Certified Internal Auditor (CIA) exam. Azerbaijan was the first FSU country to establish an IIA chapter in 1999 with 60 founder members.¹⁶

6. IRFAA Eurasia¹⁷

Introduction

Although the International Regional Federation of Accountants and Auditors Eurasia (IRFAA Eurasia) is not an Azerbaijan-based professional accountancy body, it influences accountancy developments within the FSU and within Azerbaijan.

IRFAA Eurasia was established in June 1999—its members include 20 professional accountancy organizations from 10 FSU countries. The Federation's mission is to develop and strengthen the accounting and audit profession, and promote the implementation of international professional standards and professional standards on ethics as promulgated by IFAC and IASB, through its member bodies.

The Federation provides support and assistance to national organizations of accountants and auditors in the following areas: (i) developing national organizations in preparation for IFAC recognition; (ii) ensuring high quality accounting and audit services; (iii) developing the theory and practice of accounting and audit based on international standards; (iv) preserving the professional independence of accountants and auditors; and (v) developing and strengthening professional contacts at the regional and international levels.

IRFAA Eurasia was established with, and continues to receive, support from the Organisation for Economic Cooperation and Development (OECD), the European Union (EU) and the United States Agency for International Development (USAID).

¹⁶ *Azeri Business News*. 2001 August 29. Interview with the Chairman of Chamber of Auditors of Azerbaijan. Newspaper Article.

¹⁷ Primary source: www.irfaa-eurasia.org

Azerbaijan is represented on each of the Federation's five standing committees: accounting standards, auditing standards, legal reform, membership and ethics, and professional education and certification.

Accounting Standards Committee

The Accounting Standards Committee aims to promote the harmonization of accounting practices in Eurasia through the adoption of International Accounting Standards (IAS). It also works to build public awareness, understanding and demand for IAS in the region. Its work program includes: (i) preparing a comparative analysis of national accounting standards in the Eurasian region with IAS; (ii) developing recommendations on how to implement and apply IAS; (iii) helping the translation of IAS into Russian and the distribution of these translations to the Eurasian accountancy profession; and (iv) promoting the implementation and use of IAS by public-sector organizations and educational institutions.

Auditing Standards Committee

The aim of the Auditing Standards Committee is to support IRFAA Eurasia's Member Bodies in the area of audit reform, specifically in promoting the acceptance, understanding and implementation of International Standards on Auditing (ISA), as developed by IFAC. Its work program includes: (i) coordinating the translation of ISA into Russian; (ii) establishing and maintaining contacts with IFAC's International Auditing Practices Committee (IAPC); (iii) coordinating expert examinations where requested by a Federation member; (iv) developing recommendations on the implementation and use of ISA and organize conferences on this topic; (v) publishing a guide on auditing-related matters; (vi) developing a website on audit issues; and (vi) translating IFAC's *Code of Professional Ethics*.

Legal Reform Committee

The Legal Reform Committee seeks to develop and promote model accounting and audit laws in the Eurasian region. Its work program includes: (i) creating a database on national accounting and auditing in the Eurasian region; (ii) preparing a comparative analysis between the existing national laws on accounting and auditing with international best practice; (iii) developing model laws on accounting and auditing and draft

recommendations on their implementation; (iv) establishing contacts and working relationships with respective international experts; and (v) organizing conferences and meetings with IRFAA Eurasia's Member Bodies, relevant public sector officials and international experts to discuss the implementation of the model laws on accounting and auditing in Eurasia.

Membership and Ethics Committee

The Membership and Ethics Committee aims to develop guidance on professional ethics, based on IFAC's *Code of Professional Ethics*, and to promote its acceptance, understanding and enforcement by IRFAA Eurasia's Member Bodies. In addition, it reviews applications for IRFAA Eurasia membership and monitors compliance with the Articles of Constitution. Its work program includes: (i) drafting a model Code of Professional Ethics, based on IFAC's code; (ii) preparing recommendations for IRFAA Eurasia's Member Bodies on how to implement the new ethics code; (iii) creating a computerized register of Member Bodies, including official documents, staff, membership, work program and laws; (iv) defining rules of procedure for the admittance of new Member Bodies into IRFAA Eurasia; (v) helping IRFAA Eurasia's current associate Member Bodies to become full Member Bodies, and attract new Member Bodies; (vi) visiting IRFAA Eurasia's Member Bodies to study their professional activities and monitor their compliance with membership criteria; (vii) establishing and maintaining contacts with public sector officials, international organizations and professional associations of accountants and auditors; and (viii) organizing meetings to facilitate the exchange of experience and expertise between international organizations and the professional associations of accountants and auditors situated in the Eurasia region.

Professional Education and Certification Committee

The Education Committee promotes the harmonization of professional education, training and certification programs in the Eurasia region. Based on international standards and guidelines, the Committee is developing a concept paper that will serve as a reference point for Member Body programs. Its work program includes: (i) studying and appraising current professional education and certification programs in Eurasia; (ii) drafting a model professional education and certification program, based on the relevant international education guidelines; (iii) establishing and maintaining contacts with international organizations and education in-

stitutions; (iv) drafting a strategic plan and develop recommendations on harmonization of certification and licensing programs in the Eurasian region; (v) preparing commentaries on legislative and normative acts that touch upon professional education, training, certification and licensing; (vi) assisting in the exchange of information and experience on professional education and training between IRFAA Eurasia's Member Bodies; (vii) establishing and maintaining relations with international and national organizations, and professional associations of accountants and auditors; and (viii) organizing conferences, congresses and seminars on relevant topics.

7. Issue Synopsis: Professional Infrastructure

Chapter IX—*Issues and Recommendations*—identifies and describes constraints and proposes corrective actions. These include the following issues regarding Azerbaijan's professional accountancy infrastructure:

- Licensing requirements differ from international guidelines and norms:
 - Practical experience must be relevant to licensee studies (i.e., law, finance and economics), but is not necessarily related to accounting and auditing, nor is suitable supervision required.
 - Continuing profession education (CPE) is not mandated.
- No professional stepping stones, such as the Accounting Technician qualification, exist for aspiring accountants.
- Sectoral memberships, such as for government accountants, have not yet been established.

IV. Accounting and Auditing Standards

This chapter describes the accounting and auditing standards that govern the preparation of external financial reports and the audit of those reports. It comprises seven sections as follows:

Part One: Accounting Standards

- 1 – Introduction—provides an introduction to the accounting standards that apply in Azerbaijan.
- 2 – Accounting Standard-Setting Responsibilities and Processes—describes accounting standard-setting responsibilities and processes.
- 3 – Azerbaijan Accounting Standards—describes Azerbaijan accounting standards and ongoing reform initiatives.
- 4 – Public Sector Accounting Standards—discusses the accounting standards that prevail in the public sector.
- 5 – Comparison with International Accounting Standards (IASs)—identifies differences between Azerbaijan accounting standards and IAS.

Part Two: Auditing Standards

- 6 – Azeri Auditing Standards—describes the legal status of Azerbaijan auditing standards and the process by which they are developed.
- 7 – Issue Synopsis: Accounting and Auditing Standards—summarizes the issues identified in this chapter.

Part One. Accounting Standards

1. Introduction

As related in chapter II, accounting in the FSU was designed to meet the needs of the statistical and tax authorities. It consisted of adhering to a prescribed chart of accounts that was subordinated to requirements of the central planning system and reflected the diminished scope of financial management in a centrally-planned economy. The primary function of accounting was to record factual data to assess plan accomplishments, rather than an enterprise's financial situation.

In common with most other countries transiting from the Soviet accounting system, Azerbaijan continues to emphasize uniform accounting

systems (UASs). UASs comprise sector-specific charts of accounts supported by detailed accounting rules and instructions.

In the 1990s, although the Azerbaijan Government focused on the conflict and on developing the oil and gas sector, accounting reform was accorded a low priority. Moreover, the MOF worked, and continues to work, within tight resource constraints (it has received no external technical assistance to date). Consequently, Azerbaijan's transition towards IAS-based accounting standards has generally been slower than other FSU countries.

2. Accounting Standard-Setting Responsibilities and Processes

The *Accounting Law 1995* and the *Banking Law 1996* assign accounting standard-setting responsibilities to the MOF and to the National Bank of Azerbaijan (NBA), respectively. Neither law explicitly refers to IAS. Furthermore, the Production Sharing Agreements (PSAs) exempt relevant foreign companies from following Azeri accounting standards; most of these companies use IAS.

Azerbaijan "Accounting Standards" (UASs) are developed by both the MOF and the NBA. Consultation is undertaken during the development process, through interdepartmental committees involving the Ministries of Economic Development (MOED) and Taxation (MOT). Other interested parties such as the Chamber of Auditors of Azerbaijan are also consulted. Once approved, the "standards" are registered with the Ministry of Justice in accordance with the *Law on Statutory Registration*. This final step can take many months.

3. Azerbaijan Accounting Standards

Articles 120–125 of the *Civil Code 2000* stipulate the structure of Azeri financial statements; this structure is generally inconsistent with IAS-based financial reporting.

In 1995, the MOF released updated accounting instructions and charts of account (UASs). During 2001, the MOF prepared revised UASs. The Cabinet of Ministers is currently considering the revised system, which is more consistent with IAS-based accounting. The MOF has also presented an *Accounting Reform Plan* to the Cabinet of Ministers for consideration (see Appendix 4, Appendix 5 and Appendix 6).

The *Accounting Reform Plan* reflects continuation of Soviet accounting arrangements, albeit in a manner that is more consistent with IASs. In particular, it emphasizes national accounting as a primary purpose of financial reporting. To this end, it proposes that the following UASs will be prepared during 2001–2005:

- Industrial sector (e.g., heavy industry, light industry, food industry).
- Agriculture (farmer enterprises and other agricultural fields).
- Budget organizations (education, culture, health and others).
- Extra-budgetary organizations and activities.
- Insurance organizations.
- Municipalities.
- Energy sector (e.g., water, oil, gas, electricity).
- Services (e.g., transport, communications, construction).
- Small and medium enterprises.
- Joint-stock organizations.
- Foreign individuals and organizations.
- Commerce.

In early 2000, the NBA developed and promulgated an IAS-based UAS for the banking sector. An NBA-published instructional book—*Accounting Plan for the Azerbaijan Banking System*—was released in 2001 to support the revised arrangements.¹⁸ Substantial implementation progress has been made, however much remains to be done. To this end, the World Bank is providing assistance in terms of training, advice and systems development.

The oil and gas sector is largely excluded from Azeri accounting requirements through provisions in PSAs.

4. Public Sector Accounting Standards

Azerbaijan uses sector-neutral accounting standards—with very few exceptions, accounting standards and procedures apply to both the public sector and the private sector, at the organization level. At the whole-of-government level, the International Monetary Fund (IMF) and the World Bank have supported, and continue to support, the development of cash-based budgeting and reporting, on the Government Finance Statistics (GFS) basis, in contrast to the previous practice of accrual budgeting and reporting.

¹⁸ National Bank of Azerbaijan (NBA). 2001. *Accounting Plan for the Azerbaijan Banking System*. Baku: NBA. 305 pages.

Box 1: Recommendations for the Accounting Reform in the CIS¹⁹

The Accounting Standards Committee of IRFAA Eurasia has issued guidance on IAS adoption, which is relevant to Azerbaijan circumstances, as it based on the experiences of other FSU countries. Recommendations include:

- Ensure legal support for the IAS transition process by rescinding those provisions of the regulatory acts that impede the IAS transition.
- The law should relieve entities that have adopted IAS, from submitting NAS-based financial statements. Nor should they be required to maintain dual-standards accounting records.
- Ensure that banks and other financial institutions, listed companies, their subsidiaries are required to make the transition to IAS.
- When a large state organization is offered for sale, IAS-based financial statements (preferably audited) should be prepared and included in information materials.
- An IAS transition program should be developed for enterprises that are required to be audited.
- Ensure that NASs meet the needs of small businesses and closed joint-stock companies.
- Ensure that small companies maintain accounting records in a simplified manner and prepare financial statements in accordance with the simplified version of IAS.
- Develop a system of computerized transformation entries for tax purposes, which must be used by enterprises that prepare IAS financial statements to record tax liabilities, with tax computations based on the IAS system. For small enterprises, develop a simplified system of translating financial accounting figures into performance indicators for tax purposes.
- Modify the methodologies applied by statistical authorities when collecting and analyzing enterprise financial statements so that they do not impede adoption of IASs.
- Modify national Charts of Account in accordance with IAS requirements. Do not require enterprises using IAS to apply National Charts of Account and ledger-maintenance procedures.
- Prepare and ensure the wide distribution of detailed manuals, case studies and explanations relating to the practical application of IAS.
- Ensure that there are sufficient financial resources for the reform implementation process, in particular:
 - Provide step-by-step recommendations on the transition to IAS.
 - Provide recommendations and training for enterprise employees regarding the practical application of IAS.
 - Make the necessary changes to regulatory acts of controlling authorities, whose requirements, at present, are based on NASs.

¹⁹ IRFAA Eurasia. 2001. *Recommendations for the Accounting Reform in CIS Countries*. p. 6.

5. Comparison with International Accounting Standards (IASs)

The MOF has translated IASs from Russian into Azeri. Accounting standards for the financial sector and the oil and gas sector are generally consistent with IAS.

Accounting requirements for other sectors differ substantially from IAS. These differences include: (i) financial statement formats—statements of cash flows and equity changes are not required, however, much of this information is provided elsewhere in the financial statements (in accordance with Article 31 of the *Accounting Law*); (ii) fixed asset revaluations—mandated indexing formulas are applied; (iii) contingent liabilities are not required to be disclosed; (iv) consolidation—no rules exist for the preparation of consolidated financial statements; and (v) accounting bases—although expenses must be recorded on the accrual accounting basis, revenues can be recorded on either the accruals or cash bases (where the cash basis is used, direct costs must be recorded on the cash basis in accordance with Articles 130–134 of the *Tax Code 2000*).²⁰

Part Two. Auditing Standards

6. Azeri Auditing Standards

The Chamber of Auditors of Azerbaijan promulgates auditing instructions in accordance with regulations issued under the *Auditing Services Law 1995*. These instructions are directly based on International Standards on Auditing (ISAs).

The promulgation process has the following stages:

- The Chamber of Auditors selects an ISA for consideration.
- Three external specialists are assigned to the ISA. One specialist translates the standard into Azeri, the other two review the translation and analyze the suitability of the standard for Azerbaijan.
- The standard is presented to the Board of the Chamber of Auditors of Azerbaijan for consideration. The Board identifies conflicts with Azeri laws and conditions. Where these are considered beneficial, the Board identifies consequential amendments to Azeri laws. Otherwise, the

²⁰ Partial Source: IRFAA Eurasia. 2000. *Comparison of Azerbaijan Accounting Rules with International Accounting Standards*.

conflicting provisions are removed from the standard. Once agreed, the standard is registered with the Ministry of Justice. As of December 2001, the Chamber of Auditors of Azerbaijan had reviewed, amended and promulgated 24 of the 36 ISAs (see Appendix 10).

7. Issue Synopsis: Accounting and Auditing Standards

Chapter IX—*Issues and Recommendations*—identifies and describes constraints and proposes corrective actions. These include the following issues regarding accounting and auditing standards:

- The Azerbaijan accounting standard-setting process differs from international practice; for instance, it is not prescribed in law. Moreover, standard-setting responsibilities are distributed among agencies.
- The draft, and as yet unapproved Accounting Reform Plan, reflects objectives that are largely inconsistent with accounting in a market economy—for instance, a primary purpose of financial accounting is considered to be the provision of information, in a standard format, that is needed to prepare consolidated country financial statements, which incorporate all entities, both private and public sector. The Plan also emphasizes the continued development of UASs.

V. Accounting and Auditing Training

This chapter describes accounting and auditing education and training. It is structured as follows:

- 1 – Introduction—provides an introduction to Azerbaijan accountancy education.
- 2 – Educational Legislation and Coordination—describes the coordination of Azerbaijan education and the role of legislation in setting directions for development of the education system.
- 3 – Education and Training Institutions—discusses the structure and activities of higher educational institutions in relation to accountancy education and training.
- 4 – Language of Instruction—identifies and discusses issues relating to the language of instruction.
- 5 – Professional Training Activities—describes the training activities of professional accountancy bodies.
- 6 – Other Externally-Supported Training Initiatives—describes other recent and ongoing externally-supported training initiatives.
- 7 – Issue Synopsis: Accounting and Auditing Education and Training—summarizes the issues identified in this chapter.

1. Introduction

Together with other FSU states, Azerbaijan has a high literacy rate and comparatively high educational standards. Indeed, Azerbaijan education was renowned within the Soviet Union and more widely—particularly that related to the oil and gas sectors.

However today, most higher education institutions suffer from resource constraints. This relates to teacher remuneration and the attractiveness of teaching as a career for bright graduates (the average teacher is paid \$20 per month). Infrastructures have also deteriorated considerably, due to constrained budget funding and the accommodation of refugees and internally-displaced persons in many facilities. Moreover, post-independence difficulties have constrained the development of quality academic materials including textbooks. Furthermore, computer hardware and software are lacking and high Internet fees exclude most academics and students from accessing web-based information resources.

Private education is now common in Azerbaijan. But in contrast to some other FSU countries, the quality of instruction in state education institutions is generally stronger than in private institutions. For instance, (i) nearly all of the top scorers on the state admission exam study at state institutions, and (ii) Baku State University and Foreign Language Institute students outperform their private university counterparts in the Teaching of English as a Foreign Language (TOEFL) exams.

With regards to accounting and auditing education, a significant component of accounting skills are developed through on-the-job practical training and work experience. That aside, educational standards, particularly at the undergraduate level determine the basic level of knowledge that new entrants to the accounting profession have. The higher this level is, the faster those skills will be developed. Appendix II provides details of international standards and guidelines on accountancy education.

One state institution—the State University of Economics—offers undergraduate and postgraduate accountancy programs. As of November 2001, 1,100 students were enrolled in accountancy-based bachelor programs and 90 were undertaking masters programs. The specialist schools, for instance the Oil and Gas Academy, also teach specialist accountancy studies. Eight private tertiary institutions also offer accountancy programs, two of these teach predominantly in English. Furthermore, practical accountancy training is given by 26 vocational schools.

2. Educational Legislation and Coordination

Shortly following independence, the Government recognized that the education system was largely unsuited to meet the needs of a mixed market economy; the *Law on Education* was subsequently enacted to support education reform.

The Education Ministry coordinates education activities in accordance with the *Law on Education* and with other subsidiary regulations. It directly oversees 20 of the higher educational institutions. Other ministries and committees oversee the remainder, which are predominantly specialist education institutions.²¹ The State Student Admission Committee plans and controls student-admission levels to both public and private tertiary institutes.

²¹ Ministry of Education. 2001. Higher Educational Institutions in Azerbaijan. URL: <http://edu.gov.az>

Since 1999, the Ministry of Education has reemphasized educational reform, with support from the World Bank, UNICEF and EU-TACIS. However, the system remains highly centralized.

3. Education and Training Institutions

Introduction

As of January 2001, Azerbaijan had 48 higher educational institutions (30 state and 18 private), including 26 universities, 10 academies and 12 other higher educational institutions.²²

Universities and Academies

Students generally start tertiary education after 11 years of study. Entry to degree programs is through tests administered by the State Student Admission Commission. Both public and private institutions offer four-year bachelor degree programs. Most of the state, and some of the private tertiary institutions also offer two-year masters programs and doctoral programs.

Furthermore, and although there is room for debate, many Azeris feel that the best and brightest students (i.e., those with the highest scores on the exams) end up attending the more prestigious public tertiary institutions

The *State Standards of Higher Professional Education* apply to bachelor and masters programs. The *Standards* prescribe: (i) minimum curriculum requirements; (ii) organizational structure; (iii) staff-student ratios; and (iv) protections for independence and academic freedom.

Historically, the basic education curriculum followed the FSU model, which differed substantially from a western curriculum. The curriculum must cover: general humanitarian and socioeconomic studies (20 percent); natural and applied sciences (10 percent); preparation for specialty subjects (major)(42 percent); specialty subjects (16 percent); and elective (12 percent).

One state institution—the State University of Economics—offers undergraduate and postgraduate accountancy programs. As of December 2001, 1,100 students were enrolled in accountancy-based bachelor programs and 90 were undertaking masters programs.²³ The specialist schools, for instance the Oil and Gas Academy, also teach specialist accountancy studies.

²² *Ibid.*

²³ Ministry of Education. November 2001.

Eight private tertiary institutions also offer accountancy programs, two of these teach predominantly in English. Furthermore, practical accountancy training is given by 26 vocational schools.²⁴

The quality of higher education is constrained by ad hoc curriculum development and a general absence of continuing education for accountancy lecturers and professors—the latter is critical in the dynamic environment of transitional Azerbaijan.

Vocational and Technical Education

The first Azerbaijan technical school was established in 1843 and technical education continued to develop up until transition. The facilities of technical institutions were subsequently used as accommodation for refugees and internally-displaced persons. However, since 1996, the Government has prioritized the development of technical education in order to meet the skill needs of the transition economy.²⁵

Technical education comprises: (i) one to two-year courses at the 36 vocational schools; and (ii) three-year courses at the 21 technical schools (lyceums). Twenty-four new specialties have been approved, including bookkeeper and computer operators. Practical accountancy (including bookkeeping) is taught at 26 vocational schools.²⁶

Azerbaijan Banking Training Center (ABTC)

The Baku-based Azerbaijan Banking Training Center was established, and is being developed, with EU-TACIS assistance of ●1.5 million. The Center is intended to train banking specialists in accordance with international demands. Its courses cover risk management, internal control systems and auditing, bank accounting standards and specialist auditing.

4. Language of Instruction

Russian-language education was previously the mark of excellence. Azeri-language education now dominates in accordance with Azerbaijan's move away from Russian, which includes abandonment of the Cyrillic alphabet

²⁴ *Ibid.*

²⁵ Ministry of Education. 2001. Technical and Vocational Education. URL: <http://edu.gov.az>

²⁶ Source: Ministry of Education. November 2001.

in favor of the Latin script, and the decreed use of Azeri in official and private business.

English is the new foreign language of choice. Two private universities (Khazar University and Western) use English as the language of instruction.

For accountancy in particular, there is a chronic lack of textbooks and other teaching materials. Moreover, those that are available are either outdated or unsuitable in the Azeri context. Furthermore, the ongoing transition from Russian to Azeri will limit access to textbooks and specialized materials developed in other FSU countries, or translated from other languages by FSU publishing houses.

5. Professional Training Activities

The Association of Certified Accountants of Azerbaijan (ACAAz) and the Azerbaijan Association of Entrepreneurs also conduct accounting training. Courses are based upon those of the UK Association of Certified Chartered Accountants (ACCA) and are conducted by practitioners holding ACCA trainer certificates. The Chamber of Auditors (COAA) also conducts accounting and auditing training, however some interviewees questioned the quality of these activities.

6. Other Externally-Supported Training Initiatives

Chapter VII describes donor activities.

Table 4 details particular external support to accounting and auditing education and training.

Table 4: Externally-Supported Training Activities

| Reference | Description | Timing |
|-----------|---|--------|
| EU-TACIS | The specialist Azerbaijan Banking and Training Center (ABTC) was established, and is being developed, with support from EU-TACIS (€1.5 million). EU-TACIS has also supported training for accountants and auditors through the COAA. For instance, over 100 accountants and auditors were trained in 1997 on international accounting standards and practices. | 1999– |

Table 4: Externally-Supported Training Activities (continued)

| Reference | Description | Timing |
|--------------------|---|---------|
| UNDP MAS/97/002 | Support to Human Resources Development through the National Training Council: This project, for \$21,000, helped the National Training Council to fulfill its mandated role of coordinating training in Azerbaijan. It also assisted in finalizing the design of the project and will provide initial training to Azerbaijan personnel responsible for managing the training programs. | 1997–98 |
| USAID | USAID supported accounting reform through the Chartered Association of Certified Accountants (ACCA) Training-of-Trainers and Accounting Reform Scholarship programs. Intensive training took place to convert a broad spectrum of enterprises to IAS. Due to the training, a core group of 18 Azerbaijani accountants, with USAID support, established an independent Association of Certified Accountants of Azerbaijan (ACAAz) whose goals are to promote conversion to IAS throughout the country and to develop a national certification system based on the ACAAz program. The FY 2000 program focused on further developing the Association's capacity to deliver ACAAz courses and put a certification program into place. | 2000–01 |
| World Bank | The World Bank has supported accounting training for banks and financial institutions. | 1995– |

7. Issue Synopsis: Accounting and Auditing Education and Training

Chapter IX—*Issues and Recommendations*—identifies and describes constraints and proposes corrective actions. These include the following issues regarding Azerbaijan accounting and auditing education and training:

- The ongoing transition from Russian to Azeri as the emphasized teaching language is a significant challenge for educational institutions. For accountancy in particular, there is a chronic lack of textbooks and other teaching materials. Moreover, those that are available are either outdated or unsuitable in the Azeri context.
- Computer hardware and software are lacking and high Internet fees exclude most academics and students from accessing web-based information resources.
- The quality of higher education is constrained by ad hoc curriculum development.
- There is a general absence of continuing education for accountancy lecturers and professors—the latter is critical in the dynamic environment of transitional Azerbaijan.

VI. Government Budgeting and Accounting

This chapter provides an overview of government budgeting and accounting arrangements. The ongoing World Bank Country Financial Accountability Assessment (CFAA) is focusing extensively on these arrangements and will provide more information, once completed. The chapter is structured as follows:

- 1 – Introduction—describes the governmental environment.
- 2 – Accounting Bases and Arrangements—describes the accounting bases for budgeting and reporting together with other arrangements.
- 3 – Azerbaijan Accounting Chamber (AAC)—describes the establishment and objectives of the AAC.
- 4 – Responses and Challenges—identifies progress that has been made towards improving public expenditure management arrangements.

1. Introduction

Although Azerbaijan government finances are in deficit, projected revenues from the oil and gas sector make the current situation sustainable (Table 5). Indeed the Government has established an Oil Fund and has indicated a medium-term intention to substantially reduce reliance on external assistance. The Oil Fund will support the competitiveness of the non-oil sectors and contribute to intergenerational fiscal stabilization.

However, public sector management arrangements have been characterized as inefficient, ineffective and nontransparent.

Table 5: Medium Term Budget Plan (State Budget): 1999–2005²⁷

| | 1999 Actual | 2000 Actual | 2001 Forecast | 2002 Forecast | 2003 Forecast | 2004 Forecast | 2005 Forecast |
|---------------------------|----------------|----------------|------------------|------------------|------------------|------------------|------------------|
| <i>AZM Billions:</i> | | | | | | | |
| Revenue | 2,797 | 3,572 | 4,175 | 4,620 | 5,170 | 5,720 | 6,350 |
| Expenditure | 3,245 | 3,761 | 4,595 | 5,030 | 5,510 | 6,030 | 6,630 |
| Deficit | 448 | 189 | 420 | 410 | 340 | 310 | 280 |
| <i>Percentage of GDP:</i> | | | | | | | |
| Revenue | 14.8 | 15.1 | 15.8 | 16.1 | 16.9 | 16.9 | 16.4 |
| Expenditure | 17.1 | 16.0 | 17.4 | 17.5 | 18.0 | 17.8 | 17.1 |
| Deficit | 2.4 | 0.8 | 1.6 | 1.4 | 1.1 | 0.9 | 0.7 |

²⁷ Government of Azerbaijan. 2001 May. Poverty Reduction Strategy Paper (Interim Report).

In the past two years, the Government has prioritized public expenditure management reforms. These include: (i) the ongoing development of a Medium-Term Expenditure Framework (MTEF) for use in budget preparation. Future budget submissions will provide reference to the MTEF, as well as detailed information on expenditure classifications, contingent liabilities, extra-budgetary activities, and the consolidated and general government budgets outturns for the previous year; (ii) drafting amendments to the *Budget Systems Law* and revisions to budget regulations; (iii) beginning in 2001, the publication of quarterly reports on the consolidated government budget execution, including revenues, expenditures, expenditure arrears, stock of government and government-guaranteed debts, and new loans contracted or loan guarantees issued prepared by the MOF; (iv) integration of extra-budgetary activities into the state budget beginning with the 2002 budget; and (v) strengthening the MOF internal audit function.

2. Accounting Bases and Arrangements

Government activities are generally accounted for on an accrual accounting basis at the organizational level and on a cash basis for consolidated budgeting and reporting—the cash basis was introduced with support from international institutions, particularly the IMF and the World Bank.

Government organizations prepare monthly cash reports and quarterly accrual reports that are submitted to the MOF. In 2001, the MOF began publishing consolidated quarterly reports incorporating revenues, expenditures, expenditure arrears, stock of government and government-guaranteed debts, and new loans contracted or loan guarantees issued. A revised *Budget Systems Law* has been drafted and is currently being considered.

Although government organizations are staffed with ‘accountants’ and bookkeepers, these personnel have received little ongoing training. Moreover, concerns have been raised about the suitability of their qualifications.

3. Azerbaijan Accounting Chamber (AAC)

The Azerbaijan Accounting Chamber (AAC)—Azerbaijan’s Supreme Audit Institution—was established in 2001. The Chamber’s Head was recently appointed and the 2002 budget provides resources for the Chamber’s establishment and operations. The Chamber will audit all government bodies, including all budgetary and extra-budgetary organizations and funds, and will be obligated to make public reports of its findings.

4. Responses and Challenges

Government has stated its commitment to strengthening expenditure management and accountability. This commitment is evidenced through the following activities:

- In contrast to many other transitional and developing countries, the MOF has successfully managed to gain control of bank accounts and cash arrangements.
- The Chamber of Accounts will support efforts to improve accountability and reduce corruption.
- The MOF and the MOED are together developing a Medium-Term Expenditure Framework (MTEF) to be used in preparing future budgets.
- The MOF—with IMF support—is developing a computerized treasury system that will enable publication of monthly expenditure reports within 25 days of month-end. The implementation of the system will involve extensive training for government accounting personnel.

VII. Donor Assistance

This chapter describes donor coordination mechanisms and discusses donor activities in relation to financial management and governance arrangements. It is structured as follows:

- 1 – Overview
- 2 – Coordination Mechanism
- 3 – Asian Development Bank (ADB)
- 4 – European Bank for Reconstruction and Development (EBRD)
- 5 – International Monetary Fund (IMF)
- 6 – United Nations Development Programme (UNDP)
- 7 – World Bank
- 8 – European Union (EU-TACIS)
- 9 – United States (USAID)

1. Overview

The World Bank, European Bank for Reconstruction and Development (EBRD), European Union (EU-TACIS) and the International Monetary Fund (IMF) provide significant assistance to Azerbaijan. Germany, Japan and the Netherlands are the main bilateral donors. However, the Government has announced its attention to significantly reduce its reliance on external assistance within five years.

Table 6: Overall External Assistance to Azerbaijan²⁸

| External Source (US\$ million) | 2000 Program | |
|---|--------------|-------|
| | Loan | Grant |
| Multilateral | | |
| United Nations (UN) System | .. | 6.4 |
| World Bank | 26.5 | .. |
| Other International Financial Institutions (IFIs) | 24.5 | .. |
| European Union | .. | 20.0 |
| European Bank for Reconstruction and Development (EBRD) | 75.0 | .. |
| Subtotal | 126.0 | 26.4 |
| Bilateral | | |
| Total | 50.3 | .. |
| Total | 176.3 | 26.4 |

²⁸ United Nations (UN). 2001. *Resident Coordinator Report 2000: Azerbaijan*. Baku: UN. p. 24.

2. Coordination Mechanisms

The Foreign Economic Relations Department of the Ministry of Finance coordinates external assistance to Azerbaijan. The World Bank provided assistance to enhance coordination mechanisms and policies in 1995.²⁹

3. Asian Development Bank (ADB)

Azerbaijan joined ADB in December 1999. As of December 2001, the first technical assistance project was operational³⁰ and three Project Preparatory Technical Assistances (PPTAs) were planned. ADB's assistance to Azerbaijan is intended to reduce poverty and promote socioeconomic development by supporting sustainable economic growth and assisting the poor. ADB aims to support institutional reforms that promote growth in non-oil sectors particularly agriculture and small- and medium-sized industries.

Relevant Loan Projects

As of December 2001, there were no active or planned loan projects that related directly to improving financial governance arrangements.

Relevant Technical Assistance

The relevant initiatives that ADB has supported, or is supporting, in relation to financial management and governance include:

TA No. 3661: Capacity Building for Strategic Economic Policy Formulation in the Ministry of Finance

The objective of this TA for \$762,000 approved on 31 May 2001 is to support the development of a sound economic policy framework so as to strengthen economic policy-making capacity within MOF and improve the quality of economic advice. The scope of the TA includes: (i) assistance to develop a sustainable Macroeconomic Policy Group (MPG); (ii) provision of strategic policy advice on matters of structural reform and macroeconomic policy; (iii) continuous improvement of the economic information base for

²⁹ World Bank Project P019256, *Managing Aid Coordination*, for \$350,000, 1995.

³⁰ TA No. 3661-AZE: *Capacity Building for Strategic Economic Policy Formulation in the Ministry of Finance*, for \$762,000 approved on 31 May 2001.

economic policy making within MOF; (iv) enhanced forecasting and program design capacity in MOF and improved policy analysis in key areas of fiscal reform; and (v) a macroeconomic framework and criteria for a public investment program, to be developed in coordination with MPG and the Debt Management Department of MOF, and strengthening the Project Evaluation Unit.

4. European Bank for Reconstruction and Development (EBRD)

The European Bank for Reconstruction and Development (EBRD) is emphasizing programs and activities that support privatization, financial reforms, industrial restructuring, the creation and strengthening of infrastructure, foreign investment inflows and environmental repairs. EBRD has been providing assistance to a number of organizations to improve their accounting and financial reporting capabilities.³¹

Furthermore, EBRD is currently considering providing assistance to the State Securities Committee to improve securities laws and regulations in line with international practice.

5. International Monetary Fund (IMF)

IMF has provided assistance to improve macroeconomic policies and to strengthen central bank functions.

6. United Nations Development Programme (UNDP)

United Nations (UN) activities have focused primarily on environmental issues and providing humanitarian assistance—particularly in relation to Internally Displaced Persons (IDPs) and refugees. However, UNDP is beginning to reorient away from humanitarian issues towards development.

7. World Bank

The World Bank is a significant provider of assistance to Azerbaijan. As of 30 June 2000, there were 15 operations in Azerbaijan with International

³¹ For instance, ●300,000 was provided to assist Azerbaijan Devlet Demir Yolu (State Railways of Azerbaijan) to meet loan covenants regarding accounting requirements.

Development Assistance (IDA) commitments totaling \$411 million.³² Assistance has included providing support to executing agencies to improve accounting procedures and to finance external financial audits.³³

Pipeline: Institution Building Technical Assistance Project II

This pipeline project for \$16.0 million has two components: Public Sector Reform (PSR) and Financial Sector Reform (FSR). The Public Sector Reform (PSR) component provides specific support and assistance to (i) improve the management of public resources; (ii) strengthen the accountability, efficiency and policy implementation capacity of the central government; (iii) improve the delivery of selected public services; and (iv) put in place the basic requirements for an independent judiciary and for the future development of the legal system. The Financial Sector Reform (FSR) component will focus on: (i) assistance to the Government for the divestiture of state banks; (ii) assistance to the NBA and the Government for the establishment of the necessary infrastructure, and enhancement of banking supervision; and (iii) assistance in the strengthening of the necessary legal and regulatory environment, including further improvement in the legal infrastructure, especially in relation to bankruptcy, collateral, registry of movables and related matters.

Project P055131: Second Structural Adjustment Credit Project (\$60.0 million)

The objective of this recently approved program is to support the Government's public sector reforms. In doing so, it is intended to contribute to improved public financial management, including: (i) better management of public resources—human, financial and natural; (ii) improved delivery of public services; and (iii) an enabling environment for private sector development. The proposed reform program will be a start to streamline the budget process and enhance transparency, efficiency and accountability. It will provide tools for evaluating expenditure programs and assessing trade-offs in expenditure allocation. The program to modernize public administration would lead to greater transparency, efficiency and accountability in the executive branch of the state. The legal and judicial reform program would create a framework of laws and institutions that can effectively protect private property, enforce contracts, defend economic

³² World Bank. September 2000. *Country Brief: Azerbaijan*. Wbln0018.worldbank.org/ECA/eca.nsf

³³ See for instance, Loan No. 29230: *Gas System Rehabilitation Project*, under which \$165,000 financed an external audit of Azerigaz.

rights against infringement and provide a secure environment for investments.

Tranches will be released in accordance with reform progress. Technical assistance will accompany the program. The program will address reforms in three key areas:

- **Expenditure Management and Auditing:** Many of the vital elements of a budgetary system are underdeveloped. Processes and procedures need to be established to assure that budget-funded public services are appropriate and adequate to the needs of the population, and to satisfy managerial and expenditure control requirements. A functioning internal and external audit system needs to be implemented, so that the audit entities can institute basic systems for transparency and accountability across the state and promote regularity and propriety.
- **Administrative Reform including Civil Service Reform:** The broad aim of administrative reform in Azerbaijan should be to create a government structure and workforce of the size and with the accountability, service delivery standards, transparency, skills, and incentives needed to provide quality public services and carry out the functions assigned to the state.
- **Legal and Judicial Reforms:** Stable and consistent legal framework and reliable, independent and accountable judiciary are a basic precondition for further economic development. Legal reform in Azerbaijan will concentrate on strengthening a country capacity to design a sound legal framework for market economy. This goal will be achieved through improving legal drafting processes. An independent and accountable judiciary is a crucial check on abuse of power by or in the other branches of State. Therefore judicial reform in Azerbaijan will be aimed at strengthening judicial independence, increasing efficiency and effectiveness of commercial courts and creating an enabling environment for an independent legal profession.

Loan 35180: Financial Sector Technical Assistance Loan Project (2001–2006)

This main objective of this project for \$5.4 million, approved on 12 June 2001, is to provide technical assistance to the Government of Azerbaijan to support further implementation of its financial sector development strategy. This technical assistance will focus on: (i) bank restructuring and divestiture; and (ii) enhancement of banking infrastructure and banking supervision.

Among other things, this project aims to support: (i) the introduction of IAS-based national accounting standards for commercial banks; (ii) the establishment of IAS-compatible National Accounting Standards; (iii) the passage of the required laws and regulations to enable the administration of these National Accounting Standards; (iv) the development of financial reporting by commercial banks based on the standards prescribed by NBA, and (v) the preparation of a banking manual of procedures and guidelines for accounting practices

Loan 27690: Institution Building Technical Assistance Project (1995–2001)

This project, for \$18.0 million approved on 25 July 1995, had four focal areas: (i) assisting privatization and enterprise reform; (ii) strengthening macroeconomic management; (iii) developing the financial sector; and (iv) providing legal technical assistance. The financial sector components of the project focused mainly on building the infrastructure and skills necessary for the functioning of a modern banking system, complementing the IMF's assistance for the NBA. Objectives included: (i) strengthening the payments system; (ii) developing accounting and auditing systems and standards for enterprises and banks; (iii) strengthening prudential regulations, and the bank supervision function of the NBA, and reviewing the situation in the existing large state banks and developing options on dealing with their problem portfolio; and (iv) to developing basic banking skills of core central and commercial bank staff. Among other things, this project entailed the implementation of a computerized accounting system within NBA.

8. European Union (EU-TACIS)

European Union—Technical Assistance to the Commonwealth of Independent States (EU-TACIS) priorities include: (i) supporting institutional, legal and administrative reforms; (ii) supporting the private sector and assisting economic development; (iii) alleviating the social consequences of transition; (iv) developing infrastructure networks; (v) promoting environment protection and management of natural resources; and (vi) developing the rural economy.³⁴ In relation to (ii), the assistance program is focusing attention on the development of internationally-accepted accounting standards

³⁴ European Union. 2000. *Republic of Azerbaijan: 2000-2003 Indicative Programme*. p. 20.

9. United States (USAID)

Although the activities of the United States Agency for International Development (USAID) have, until recently, been limited, USAID is providing assistance to support the introduction of international accounting standards and to develop qualified Azeri financial experts in order to facilitate a country-wide transfer to international standards of financial reporting.

In particular the project to support the Association of Certified Accountants of Azerbaijan includes: (i) training specialists and producing printed training materials; (ii) introducing a system of accounting certification; (iii) organizing ongoing courses for accounting certification; (iv) expanding the Accounting Association's activities into the four regions of Azerbaijan.³⁵

³⁵ B01-0035, Support to the Association of Certified Accountants of Azerbaijan for \$25,000.

VIII. Issues and Recommendations

This chapter presents the issues and recommendations that are associated with gaps or weaknesses in accounting and auditing arrangements. These recommendations are intended to supplement and support existing strategies and projects. This study concludes that, with some exceptions, much remains to be done to align Azerbaijan accounting and auditing arrangements with international practices and with the needs of the mixed market economy.

These changes include developing a supportive and appropriate legislative and institutional environment, reforming accounting standards and strengthening the accounting and auditing profession—internationally-compatible arrangements can only be successfully implemented with the support of a strong profession comprising skilled accountancy professionals.

Azerbaijan is in a position to examine the reform experiences of other FSU countries and, by doing so, to develop a cohesive road map for accountancy reform that (hopefully) will enable it to avoid the errors made by other countries. To this end, this DSAA recommends that a coordination group be established to: (i) develop a strategic plan for accountancy reform; and (ii) design and agree to a legislative and institutional framework that will support implementation of the strategic plan.

The issues and recommendations are divided into two parts as follows.

- Part One: Where the matter referred to may be considered and, if any action is to be taken, this would be better achieved with external assistance.
- Part Two: Where the matter referred to may be considered and, if any action is to be taken, this may be achieved without the need for external assistance.

Part One. Where Donor Assistance Might be Appropriate

1. Establish Coordination Group, Develop Strategic Plan and Review Framework

In addition to conflicts between governing legislation, some laws will impede development of accounting arrangements. Moreover, assignments of institutional responsibilities are inappropriate in some cases. Finally, there is much to be done regarding accountant certification and general accounting training.

Although the MOF has prepared the draft *Accounting Reform Plan* covering legislation, management accounting, internal auditing and external auditing, it has done so within its limited resources. In general, the development of financial management arrangements is fragmented with several organizations taking initiatives. A high-level, representative coordination group could do much to ensure that these efforts are mutually supportive and do not overlap or conflict.

It is **recommended** that assistance be provided to support financial management developments, through establishment of a Coordination Group.

It is also **recommended** that assistance be provided to assist the Coordination Group to prepare a strategic plan for the development of Azeri accounting and auditing. The project would involve: (i) researching Azerbaijan accounting and auditing arrangements; (ii) identifying and analyzing existing problems; (iii) examining and drawing useful lessons from regional and international experience in terms of developing financial management arrangements; and (iv) using this information and the associated analyses to formulate a medium- to long-term development plan for Azerbaijan financial management.

It is further **recommended** that assistance be provided to assist the Coordination Group to review the legislative, regulatory and institutional framework and to identify necessary changes to this framework.

2. Amend Laws and Regulations

Among other things, the prescriptive provisions of the *Civil Code 1999* conflict with the adoption of international accounting practices. Several laws are currently under revision including the *Accounting Law 1995* and the *Banking Law 1996*.

It is **recommended** that assistance be provided to develop a legislative base that is conducive to the adoption of international accounting and auditing practices.

3. Clarify Accounting Standard-Setting Arrangements

The MOF and ANB both promulgate Azeri accounting standards in accordance with a Presidential Decree.

It is **recommended** that the *Accounting Law 1995* be revised to support the development of accounting standard-setting arrangements.

4. Clarify Legal Status of Auditing Standards

Relevant Azeri laws are largely silent regarding auditing standard requirements.

It is **recommended** that all laws requiring audited financial statements be amended to stipulate that these audits must be conducted in compliance with Azeri auditing standards and practices.

5. Clarify Auditing Standard-Setting Arrangements

COAA sets Azeri auditing standards. However, the standard-setting process is not enshrined in law. For instance, the composition of the standard-setting body should be legally established (regulators and financial statement users should be strongly represented).

It is **recommended** that the *Accounting Law 1995* be revised to provide for the development of auditing standard-setting arrangements.

6. Broaden and Strengthen Accounting Qualifications

COAA issues audit licenses to individuals and to auditing firms. The licensing process could be strengthened significantly. The revised accounting law, prepared by the MOF, envisages that this responsibility would be assigned to the MOF. Furthermore, while the Chamber has one membership category (licensed auditor), it is common international practice for professional bodies to have a range of membership categories with differing qualification criteria including Accounting Technicians, Management Accountants, Government Accountants and CPAs. The establishment of additional membership categories, with appropriate qualification criteria, would strengthen the Azeri accounting profession and broaden the Chamber's membership and revenue base.

It is **recommended** that assistance be provided to establish additional accounting qualifications including Accounting Technician, Management Accountant, Internal Auditor, Government Accountant and CPA.

It is also **recommended** that assistance be provided to: (i) review existing licensing procedures and requirements (e.g., education, practical experience and professional examinations); (ii) develop improved licensing procedures and requirements, and (iii) implement these new licensing procedures.

It is further **recommended** that individuals already holding audit licenses be required to re-qualify under the improved qualifications when their existing licenses expire.

7. Develop Training Materials

The COAA has developed training materials with EU-TACIS assistance. However, the rapidly changing environment and need for professional development present major challenges. Multimedia and Internet-based technologies present options to prepare effective interactive training materials that are easily redeveloped to reflect the changing environment and can easily be distributed to far-flung regions.

It is **recommended** that assistance be provided to develop training materials for accountant continuing professional education. Similar ongoing ADB-supported initiatives for the People's Republic of China, Nepal and the Philippines are directly relevant. The project would involve: (i) studying options for preparing and providing training materials to CPAs; (ii) developing a medium- to long-term plan for developing continuing professional education; (iii) studying options for developing and delivering training materials using modern technology, and (iii) developing training materials and training trainers.

8. Develop Accounting Curriculum and Materials

The move towards Azeri-language instruction combined with the rapidly changing accounting environment means that quality accounting educational materials are not generally available. Moreover, the academic curriculum has not kept pace with environmental changes.

It is **recommended** that assistance be provided to: (i) review the accounting curriculum; (ii) revise the accounting curriculum; (iii) prepare suitable accounting textbooks and other training materials, and (iv) implement the new curriculum in universities.

9. Provide Continuing Training to Professors and Lecturers

Azerbaijan has extremely competent accounting professors and lecturers due to the country's legacy of high educational standards. However, not all these professors and lecturers are conversant with the changes in the accounting environment.

It is **recommended** that assistance be provided to design and implement a continuing education program for accounting lecturers and professors.

10. Establish Government Accountant and Auditor Certifications

As described above, professional qualifications for government accountants should be established. Furthermore, the recently established AAC intends to develop certification procedures and associated training programs for its auditors.

It is **recommended** that assistance be provided to develop certification procedures and associated training programs for government accountants and auditors.

Part Two. Where External Assistance is Not Required

All recommendations would best be implemented with external assistance.

IX. Main Deficiencies and Action Plan

Azerbaijan's financial management reforms lag behind those of most other Former Soviet Union countries. However, it is now positioned to closely examine other countries' efforts and, by doing so, to develop a comprehensive strategy for effective reform. Issues and recommendations may be categorized as follows:

- Those deficiencies that are better able to be resolved with external assistance; and
- Those deficiencies that are able to be resolved without the need for external assistance.

| Action | Priority | Donor Assistance? | Country Support? | 2002 - 2006 |
|---|----------|-------------------|-------------------|-------------|
| Establish Coordination Group, Develop Strategic Plan and Review Framework | High | ✓ | ... ³⁶ | ■ |
| Amend Laws and Regulations | High | ✓ | ✓ | ■■■ |
| Clarify Accounting Standard-Setting Arrangements | High | ✓ | ✓ | ■■■ |
| Clarify Legal Status of Auditing Standards | High | ✓ | ✓ | ■■■ |
| Clarify Auditing Standard-Setting Arrangements | High | ✓ | ✓ | ■■■ |
| Broaden and Strengthen Accounting Qualifications | High | ✓ | ✓ | ■■■■ |
| Develop Training Materials | High | ✓ | ✓ | ■■■■■ |
| Develop Accounting Curriculum and Materials | High | ✓ | ✓ | ■■■■■ |
| Provide Continuing Training to Professors and Lecturers | High | ✓ | ✓ | ■■■■■ |
| Establish Government Accountant and Auditor Certifications | High | ✓ | ✓ | ■■■■■ |

³⁶ This recommendation was strongly supported by all Baku workshop participants (5-6 December 2001), but there was mixed support at the Manila workshop (5-6 March 2002).

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Appendix 1. Useful Internet Sites

1. General Information on Azerbaijan

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| Azerbaijan Internet Links | http://resources.net.az |
| Azerbaijan Online | http://azerbaijan-online.com |
| Azerbaijan Yellow Pages | www.yellowpages.top.az |
| United States-Azerbaijan Chamber of Commerce (USACC) | www.usacc.com |

2. Regulatory and Standard-Setting Bodies

| | |
|---|--|
| Bank for International Settlements (BIS) | www.bis.org |
| International Accounting Standards Board (IASB) | www.iasc.org.uk |
| International Federation of Accountants (IFAC) | www.ifac.org |

3. Professional Bodies

| | |
|---|--|
| Association of Certified Accountants of Azerbaijan (ACAAz) | www.acaaz.org |
| Confederation of Asian and Pacific Accountants (CAPA) | www.capa.com.my |
| Georgian Federation of Professional Accountants and Auditors | www.gfpaa.kheta.ge |
| International Regional Federation of Accountants and Auditors Eurasia (IRFAA Eurasia) | www.irfaa-eurasia.org |
| Chamber of Auditors of the Republic of Kazakhstan | www.audit.freenet.kz |
| Association of Professional Accountants and Auditors of the Republic of Moldova | www.acap.ngo.moldnet.md |
| Russian College of Auditors | www.rka.org.ru |
| Union of Accountants and Auditors of Kyrgyzstan | www.oba.kg |
| Ukrainian Federation of Professional Accountants and Auditors | www.ufpaa.kiev.ua |

4. International Organizations

| | |
|--|---|
| Asia Pacific Economic Cooperation (APEC) | www.apecsec.org.sg |
| Financial Stability Forum | www.fsforum.org |
| International Federation of Accountants (IFAC) | www.ifac.org |
| International Organization of Securities Commissions (IOSCO) | www.iosco.org |
| International Organization of Supreme Audit Institutions (INTOSAI) | www.intosai.org |
| Open Society Institute – Assistance Foundation (OSI-AF) Azerbaijan | www.ozl-az.org |
| UN Conference on Trade and Development (UNCTAD) | www.unctad.org |
| UNCTAD Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) | www.unctad.org/en/subsites/dite/ 3_edev/3_isarac.htm |
| World Trade Organization (WTO) | www.wto.org |

5. Government Organizations

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|---|---|
| Ministry of Education | http://edu.gov.az |
| Ministry of Economic Development (MED) | http://economy.gov.az |
| National Bank of Azerbaijan (NBA) | www.nba.az |

6. Accounting Firms

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|--|--|
| Andersen | www.andersen.com/azerbaijan |
| Central Asia Business Consultants (associated with Deloitte Touche Tohmatsu) | www.cabc.top.az |
| Ernst & Young | www.eycis.com |
| KPMG | www.kpmg.az |
| PricewaterhouseCoopers Eastern Europe BV | www.pwcglobal.com |

7. Financial Organizations

| | |
|---|--|
| Promtekhbank Joint-Stock Commercial Bank | www.ptbank.com |
| Arkobank | www.arkobank.top.az |

| | |
|--|---|
| AzeriGazBank | http://intrans.baku.az/bicex/agb/agb_ind.htm |
| Debut Bank | www.az/debut |
| Insurance Companies in Azerbaijan (Listing) | www.atlas.com.ru/cmp/azer.html |
| International Bank of Azerbaijan | www.ibar.az |
| Royal Bank | www.rbb.azeri.com |
| SIB – Azerbaijan Industrial Investment Join-Stock Commercial Bank | www.sib-az.com |

8. Educational Institutions and Providers

| | |
|-----------------------|--|
| Ministry of Education | http://edu.gov.az |
| Western University | www.wu.aznet.org/CI_SBA.HTM |

9. Donor Organizations

| | |
|--|--|
| Asian Development Bank (ADB) | www.adb.org |
| Canadian International Development Agency (CIDA) | www.acdi-cida.gc.ca |
| EU-TACIS | www.europa.eu.int/comm/index.htm |
| European Bank for Reconstruction and Development | www.ebrd.org |
| German Technical Assistance Agency: Gesellschaft für Technische Zusammenarbeit (GTZ) | www.gtz.de |
| International Monetary Fund (IMF) | www.imf.org |
| Islamic Development Bank (IsDB) | www.isdb.org |
| Japan Bank for International Cooperation (JBIC) | www.jbic.go.jp |
| Japan International Cooperation Agency (JICA) | www.jica.go.jp |
| Netherlands | www.minbuza.nl |
| Organisation for Economic Cooperation and Development (OECD) | www.oecd.org |
| United Nations Development Programme (UNDP) | www.un-az.org/undp |
| United Kingdom Department for International Development (DFID) | www.dfid.gov.uk |
| United States Agency for International Development (USAID) | www.usaid.gov |
| World Bank | www.worldbank.org |

Appendix 2. Interviewees

Aspects of financial management and governance were discussed with the following people.

| | | |
|-----------------------------|---|---|
| Abbas Allahverdiyev | Deputy Chair | Azerbaijan Chamber of Accounting |
| Professor Vahid T. Novruzov | Chair | Chamber of Auditors of Azerbaijan |
| Gasham H. Bayramov | Director | Chamber of Auditors of Azerbaijan, Department of Standardization |
| Elkhan Jafarov | Head | Ministry of Finance, Accounting Policy Department |
| Ismailiylov Sabir | (Former) Chair | Ministry of Finance, Accounting Policy Department |
| Kamalya Humbatova | Officer | Ministry of Finance, Accounting Policy Department |
| Mardan H. Mardanov | Head | Ministry of Finance, Foreign Economic Relations Department |
| Adalet N. Aliyev | Head | Ministry of Finance, Foreign Economic Relations Department, Asian Region Relations Division |
| Robert Rudy | Economic Advisor | Ministry of Finance, Macroeconomic Policy Group |
| Abdul M. Khan | Resident IMF Treasury and Computerization Advisor | Ministry of Finance, Treasury Department |
| Zahir Abdullaev | Officer | Ministry of Finance, Treasury Department |
| Peter Burnie | Partner | Arthur Andersen MMM |

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| | | |
|-----------------------|----------------------------------|---|
| Faraj Huseynbeyov | Azerbaijan Liaison Officer | Asian Development Bank |
| Marco Gatti | Senior Programs Officer | Asian Development Bank |
| Gulnara Alekberova | Chief Coordinator | Association of Certified Accountants of Azerbaijan (ACAAz) |
| Fuad S. Ibrahimov | Staff Chief | Azerbaijan Accounting Chamber (AAC) |
| Salim Kriman | Vice President | Baku Stock Exchange |
| Lala Rzayeva | Senior Programs Officer | Eurasia Foundation |
| Gregory D. Stephenson | Outreach Coordinator | Eurasia Foundation |
| Michael Mered | Resident Representative | International Monetary Fund (IMF), Azerbaijan Resident Mission |
| Peter Barrand | IMF Technical Assistance Advisor | Ministry of Taxation |
| Rufat C. Aslanov | Director | National Bank of Azerbaijan (NBA), Banking Supervision Department |
| Muhmmad Ismail | Finance and Systems Manager | Pepsi Azerbaijan |
| Kenny Hawsey | Partner | PricewaterhouseCoopers |
| Geir Jøssang | Senior Vice President | Statoil (Norway), International Development and Production |
| Farid Mamedov | Operations Officer | World Bank , Azerbaijan Country Office, Infrastructure and Energy Sector Unit |
| Rochelle Hilton | Operations Officer | World Bank, Private and Financial Sector Development, Europe and Central Asia |

Appendix 3. RETA 5980 (Regional Study) Information

1. Study Phases

The study had three broad phases as follows:

Phase I – Azerbaijan Case Study on Accounting and Auditing Support and Structures.

Phase II – Baku Workshop (5-6 December 2001).

Phase III – Manila Workshop (5-6 March 2002) and Formulation of Action Plan.

2. Phase I : Case Study On Accounting and Auditing

This phase involved the examination of Azerbaijan's current accounting and auditing structure and systems. It also (i) analyzed Azerbaijan's political, institutional, and regulatory and legal framework on accounting and auditing practice and the level of enforcement of existing laws, rules, and regulations; (ii) identified gaps and weaknesses in accounting and auditing support available and deviations from international standards; and (iii) identified alternative options to remedy the identified weaknesses, with the objective of eventually doing away with these.

Barry Reid and Nailya Ablieva conducted the fieldwork for the study from 5 November to 3 December 2001. Financial management and governance arrangements were discussed with representatives from: the Ministry of Finance (MOF), the Chamber of Auditors of Azerbaijan (COAA), the Azerbaijan Accounting Chamber (AAC), other government organizations, private sector businesses and educational institutions. A list of interviewees is attached as Appendix 2.

3. Phase II : Baku Workshop

Issues arising from the study were discussed and debated at a workshop held in Baku on 5-6 December 2001. Prof. Vahid T. Novruzov (Chair, COAA) and Mr. Ismailiylov Sabir (Chair of the Accounting Policy Department, MOF) opened the workshop. Francis B. Narayan, Lead Financial Management Specialist, ADB, participated in the workshop as a resource person and provided overall guidance with respect to the objectives of the Study. Around 25 participants attended the workshop.

4. Phase III : Formulation of Action Plan

Phase III assessed the roles that ADB and other funding agencies could play in improving the current situation in the selected DMCs. The roles included policy intervention, projects and program assistance, and

mobilization of cofinancing resources to address the identified problems and weaknesses. This activity was undertaken in close consultation with the Government, regulatory authorities, representatives of the accounting and auditing professions, and other local interest groups and funding agencies. At this stage of the RETA, the commitment-in-principle of each selected country to implement the findings and recommendations of the study was agreed. The findings of the RETA were disseminated and debated at a workshop in Manila on 5-6 March 2002 and the developed action plan was finalized for implementation.

Appendix 4. Draft Presidential Decree on Accounting Reforms

The following Presidential Decree was prepared and submitted by the MOF in 2000. It has not yet been approved.

State Program of National Accounting Standards (NASs) and Accountancy Reforms in the Republic of Azerbaijan in 2001-2005 (see Appendix 5 and Appendix 6).

- To ensure that NASs conform with international standards and to speed up accounting reforms in the Republic of Azerbaijan, I have decided:
- To approve the State Program of National Accounting Standards (NASs) and accountancy reforms in the Republic of Azerbaijan in 2001-2005.
- The administration for implementation of the State Program and coordination of the work of professional specialists engaged in implementation on the basis of contracts is to be carried out by the Ministry of Finance (MOF)
- Although drafting the State budget for 2002-2005, the MOF should reserve funds necessary for implementation of measures envisaged in the State Program
- The Cabinet of Ministers is responsible for resolving all matters relating to this Decree.

Appendix 5. State Program of National Accounting Standards (NASs) and Accountancy Reforms in the Republic of Azerbaijan in 2001-2005

The following program was submitted with the draft Presidential Decree (see Appendix 4 and Appendix 6) in 2000. It has not yet been approved.

1. General

This program aims to support development of a national accounting system that is compatible with the needs of Azerbaijan's market economy transition. This includes: (i) modifying accounting arrangements to support economic development by improving the transparency of government finances and improving taxation assessment and collection; (ii) preparing legislation and regulations that align with international standards; and (iii) improving the availability and accuracy of economic information to facilitate analyses of reform effectiveness.

Accounting reforms are required as part of the transition process. An important objective is to ensure control over accounting policies and arrangements through developing NASs and other guidance materials.

Accounting arrangements are very important to economic development. It is essential that highly skilled accounting professionals be developed. This will require the preparation of education materials (e.g., educational programs, learning materials, books, etc).

A critical element is developing a program to automate national accounting based upon NASs, so as to ensure efficiency and the timely availability of information.

2. Main Purposes of Implementing the Reforms

The main purposes of implementing the reforms are to:

- collect complete and accurate information on the financial and economic activities of individuals and organizations, and for preparing accounting reports for the effective enterprise management by heads of enterprises, founders, entrepreneurs, financial, banking, tax and insurance bodies, investors, state bodies and other organizations and persons.
- ensure control over: (i) property and its usage; (ii) property rights and commitments; (iii) labor and material usage; and (iv) financial resources, according to approved norms, standards and estimates.
- enable timely avoidance of financial and economic problems and to ensure that internal resources are used effectively.

- correctly determine Azerbaijan's GDP, assets and liabilities.
- guarantee timely and accurate information for government purposes.
- ensure financial transparency and to accurately identify taxable income.
- ensure the accuracy of financial reports.
- create the conditions for effective accounting arrangements.
- gradually make NASs compatible with International Accounting Standards.
- automate accounting.
- utilize the accounting experience of international organizations.

3. Reform Components and the Scope of National Accounting Standards

In accordance with market economy requirements and international standards, the main reform directions are:

- improving legal and other normative regulations.
- preparing standards and operational materials and instructions (e.g., accounting registers, accounting report formats and instructions, rules, methodic material and commentaries).
- developing computerized accounting information systems that are compatible with NASs.
- developing personnel (strengthening accounting professionals).
- enhancing cooperation with international organizations.
- preparing the NASs and attracting individuals and organizations to the accountancy profession.

Where appropriate, existing accounting arrangements and traditions should be preserved during the gradual transition to international standards. When developing legal arrangements in line with international standards, the following points should be ensured:

- To prepare amendments to the Law on Accounting and other laws and regulations.
- To prepare and approve NASs that are broadly consistent with IASs within two years.
- To revise all accounting guidance and instructional materials.
- To prepare a simplified accounting system for small enterprises within two years.

Other tasks, in addition to those in the State Program, should be defined by the MOF. To ensure the implementation of the State Program, the MOF

has the right to recruit specialists on a contractual basis NASs prepared during 2001–2005 will cover:

- Industrial sector (e.g., heavy industry, light industry, food industry).
- Agriculture (farmer enterprises and other agricultural fields).
- Budget organizations (education, culture, health and others).
- Extra-budgetary organizations and activities.
- Insurance organizations.
- Municipalities.
- Energy sector (e.g., water, oil, gas, electricity).
- Services (e.g., transport, communications, construction).
- Small and medium enterprises.
- Joint-stock organizations.
- Foreign individuals and organizations.
- Commerce.

The NASs will apply to the operational activities of all individuals and organizations within Azerbaijan.

Appendix 6. Implementation Plan for State Program of Accounting Reform

The following implementation plan was submitted with the draft Presidential Decree (see Appendix 4 and Appendix 5) in 2000. It has not yet been approved.

1. Legal Amendments

| Activity | Timing | Responsibility |
|--|-----------|---|
| <ul style="list-style-type: none"> • Identifying and preparing amendments to the Law on Accounting or preparing a new draft | 2001-2005 | MOF and involved professional specialists |
| <ul style="list-style-type: none"> • Identifying and preparing amendments to other legislation and regulations | 2001-2005 | MOF and involved professional specialists |

2. Amending Uniform Accounting Systems (Guidance and Instructions)

| Activity | Timing | Responsibility |
|--|--------|---|
| <ul style="list-style-type: none"> • Amending the accounting plan for budgetary bodies and preparing new instructions for its application | 2001 | MOF and involved professional specialists |
| <ul style="list-style-type: none"> • Financial accounts in Budgetary bodies and preparation of its new compiling rules | 2001 | MOF and involved professional specialists |
| <ul style="list-style-type: none"> • Preparation of "Charter" on accounting | 2002 | MOF and involved professional specialists |
| <ul style="list-style-type: none"> • Accounting plan in economy bodies and preparation of new instruction for its application | 2002 | MOF and involved professional specialists |
| <ul style="list-style-type: none"> • Financial accounts in economy bodies and preparation of new compiling rules | 2002 | MOF and involved professional specialists |
| <ul style="list-style-type: none"> • Accounting plan in insurance bodies and preparation of instruction for its application | 2003 | MOF and involved professional specialists |

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| Activity | Timing | Responsibility |
|--|-----------|---|
| • Financial accounts in insuring bodies and preparation of new compiling rules | 2003 | MOF and involved professional specialists |
| • Preparation of other accounting standards in connection with insurance | 2003 | MOF and involved professional specialists |
| • Preparation of an exemplary “Charter” on accounting policy | 2001 | MOF and involved professional specialists |
| • Simplified rules of accounting at the small entrepreneurship establishments | 2001 | MOF and involved professional specialists |
| • Account of non-material activities | 2002 | MOF and involved professional specialists |
| • Account of “Original resources” | 2002 | MOF and involved professional specialists |
| • Account of “Leasing” operations | 2002 | MOF and involved professional specialists |
| • Account of “Equipment to be installed” | 2001 | MOF and involved professional specialists |
| • Account of “Financial investments” | 2001 | MOF and involved professional specialists |
| • Account of “Capital investments” | 2003 | MOF and involved professional specialists |
| • Account of “Stale” (amortization) | 2004 | MOF and involved professional specialists |
| • Account of “Stocks” | 2003 | MOF and involved professional specialists |
| • Package and package operations | 2004 | MOF and involved professional specialists |
| • Account of “Means” | 2003 | MOF and involved professional specialists |
| • Account of “Currency operations” | 2001-2005 | MOF and involved professional specialists |
| • Account of “Securities” | 2001-2005 | MOF and involved professional specialists |
| • Account of animal breeding | 2004 | MOF and involved professional specialists |
| • Account of plant growing | 2004 | MOF and involved professional specialists |
| • Preparation of the other accounting standards in connection with farming economy | 2002 | MOF and involved professional specialists |

DIAGNOSTIC STUDY OF ACCOUNTING AND AUDITING PRACTICES IN AZERBAIJAN

| Activity | Timing | Responsibility |
|--|--------|---|
| • Account of “Property estimation and over-estimation” | 2002 | MOF and involved professional specialists |
| • Account of expenditures of “Original production” | 2003 | MOF and involved professional specialists |
| • Account of circulating expenditures | 2003 | MOF and involved professional specialists |
| • Account of expenditures of “Servicing economies” | 2002 | MOF and involved professional specialists |
| • Preparation of the other accounting standards in connection with the production expenditures | 2005 | MOF and involved professional specialists |
| • Account of expenditures on “Investigation and construction” | 2005 | MOF and involved professional specialists |
| • Account of settings with “Budget” | 2002 | MOF and involved professional specialists |
| • Account of settings for “Off-budget funds” (payments) | 2003 | MOF and involved professional specialists |
| • Account of settings for “Social insurance and guarantees ” | 2004 | MOF and involved professional specialists |
| • Account of productions, goods, works and services | 2005 | MOF and involved professional specialists |
| • Account of turnover expenditures | 2005 | MOF and involved professional specialists |
| • Preparation of the other accounting standards in connection with commercial organizations | 2005 | MOF and involved professional specialists |
| • Account of settings with work staff on “Labor payment and other operations” | 2003 | MOF and involved professional specialists |
| • Account of settings with the founders | 2003 | MOF and involved professional specialists |
| • Accounts of settings with “Intra-economy” and reproduction (dependent) enterprises | 2003 | MOF and involved professional specialists |
| • Account of settings with “debtors and creditors” | 2004 | MOF and involved professional specialists |
| • Inventory of property and obligations | 2002 | MOF and involved professional specialists |

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| Activity | Timing | Responsibility |
|---|-----------|---|
| • Account of “Benefit and loss” | 2002 | MOF and involved professional specialists |
| • Compiling rules of accounting at the municipalities | 2005 | MOF and involved professional specialists |
| • Compiling rules of accounting in building organizations | 2005 | MOF and involved professional specialists |
| • Account of capitals (funds) and stocks | 2004 | MOF and involved professional specialists |
| • Account of credits, debts and special financing | 2004 | MOF and involved professional specialists |
| • Account of off-balance operations | 2001 | MOF and involved professional specialists |
| • Preparation of requisitions and forms of modern initial account documents on areas | 2001-2005 | MOF and involved professional specialists |
| • Preparation of requisitions and forms of modern accounting registers on areas | 2001-2005 | MOF and involved professional specialists |
| • Preparation of methodical instructions on expenditures in connection with production and sale of work and service | 2005 | MOF and involved professional specialists |
| • Preparation of the other normative and juridical acts in connection with accounting | 2001-2005 | MOF and involved professional specialists |

3. Computerized Accounting Information Systems

| Activity | Timing | Responsibility |
|--|--------|---|
| • Preparing a computer program to automate accounting using the new accounting standards | 2005 | MOF and involved professional specialists |

4. Professional Development and Training

| Activity | Timing | Responsibility |
|---|--------|--|
| • Preparing a professional code of ethics for accountants | 2005 | MOF, Ministry of Education and involved professional specialists |
| • Preparing educational materials | 2005 | MOF, Ministry of Education and involved professional specialists |

DIAGNOSTIC STUDY OF ACCOUNTING AND AUDITING PRACTICES IN AZERBAIJAN

| Activity | Timing | Responsibility |
|---|--------|--|
| <ul style="list-style-type: none">• Preparing other instructional materials and educational programs for accounting specialists | 2005 | MOF, Ministry of Education and involved professional specialists |

5. International Cooperation

| Activity | Timing | Responsibility |
|---|-----------|----------------|
| <ul style="list-style-type: none">• Membership of the International Accounting Standards Committee (IASC) | 2001-2005 | MOF |
| <ul style="list-style-type: none">• Cooperation with the Organisation for Economic Cooperation and Development (OECD) | 2001-2005 | MOF |
| <ul style="list-style-type: none">• Cooperation with the International Federation of Accountants (IFAC) | 2001-2005 | MOF |

Appendix 7. International Standards and Guidelines on Professional Arrangements

1. Overview

The IFAC Board created a Compliance Committee in May 2000. The Committee is one of several initiatives designed to strengthen IFAC and the international profession. Its primary responsibilities are: (i) monitoring the relevance, sufficiency, and efficacy of IFAC membership obligations; (ii) monitoring member body compliance with these obligations; (iii) recommending actions to the IFAC Board and Council in respect of membership obligations; (iv) reviewing the investigative and disciplinary processes of member bodies, and reporting and making recommendations on these to the IFAC Board and Council; (v) considering how member bodies might best be encouraged, or if necessary, required to comply more closely with such obligations; (vi) devising schemes to assist member bodies to comply more closely and to considering whether additional powers are required to enforce compliance with membership obligations; and (vii) implementing agreed policy in this area. The Compliance Committee will also work closely with members of the Transnational Audit Committee (TAC) in its monitoring of the members of the IFAC Forum of Firms (FOF) once these entities are fully established.

Table 7 sets out relevant international guidelines with respect to the accountancy profession. IFAC has also established a *Money Laundering Task Force*. The task force has obtained information from around the world on what other professional bodies are doing and is currently analyzing these activities. This is a first step in determining its scope of activities. Included in the work of the task force will be consideration of whether standards will be developed to help member bodies and their members to address money laundering and related issues.

Table 7: International Guidelines for the Accountancy Profession

| | |
|---|--|
| World Trade Organization (WTO): General Agreement on Trade in Services (GATS) | The criteria for recognizing professional qualifications may not exceed what is necessary to ensure the quality of service. Each country is expected to have a methodology for comparing professional qualifications and this must be applied in a fair and consistent manner to all applicants. |
|---|--|

Table 7: International Guidelines for the Accountancy Profession (continued)

| | |
|---|--|
| Confederation of Asian and Pacific Accountants (CAPA) | CAPA's Guide on the Essential Components of a Professional Accountancy Body ³⁷ covers: (i) Admission / Advancement Standards; (ii) Full Membership Requirements; (iii) Continuing Professional Education (CPE); (iv) Technical Standards; (v) Quality Assurance / Peer Review Program; (vi) Registration as Accountant/Auditor; (vii) Disciplinary Rules; (viii) Management and Administrative Structures; (ix) Governance; and (x) External Affiliations / Memberships. ³⁸ |
| International Federation of Accountants (IFAC) | <p>IFAC pronouncements cover several areas:</p> <ul style="list-style-type: none"> • Education Guidelines and Standards. IFAC's Education Committee issues International Education Standards (IESs) and International Education Guidelines (IEGs). The IESs are intended to establish the essential elements on which education and training programs, both prequalification and postqualification, for all accountants should be founded. The IEGs promote good practice and or provide good advice. They are based on careful study of the best practices and most effective methods for dealing with the issues being addressed. • Code of Ethics for Professional Accountants. This is intended to serve as a model on which to base national ethical guidance. It sets standards of conduct for professional accountants and states the fundamental principles that should be observed by professional accountants in order to achieve common objectives. • Statement of Policy of Council: Implementation and Enforcement of Ethical Requirements.³⁹ This statement sets expectations and provides guidance on disciplinary action, including punishment and publicity. • Assuring the Quality of Professional Services. This statement sets expectations on quality control policies and procedures for member bodies and professional firms.⁴⁰ |

³⁷ Confederation of Asian and Pacific Accountants (CAPA). 1998. *Guide on the Essential Components of a Professional Accountancy Body*.

³⁸ Further details are provided in: Narayan, Francis B., Ted Godden, Barry Reid, and Maria Rosa Ortega. 2000. *Financial Management and Governance Issues in Selected Developing Member Countries: A Study of Cambodia, People's Republic of China, Mongolia, Pakistan, Papua New Guinea, Uzbekistan, and Viet Nam*. Asian Development Bank. p. 27.

³⁹ International Federation of Accountants (IFAC). 1998 January. *Statement of Policy of Council: Implementation and Enforcement of Ethical Requirements*. New York: IFAC.

⁴⁰ International Federation of Accountants (IFAC). 1999 August. *Assuring the Quality of Professional Services*. New York: IFAC.

Table 7: International Guidelines for the Accountancy Profession *(continued)*

| | |
|--|--|
| Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) of the UNCTAD | <p>In February 1999, UNCTAD issued a report on accounting education and qualifications.⁴¹ The report provides a useful set of benchmarks in respect of these issues, in particular:</p> <ul style="list-style-type: none"> • Guideline for a Global Accounting Curriculum and Other Qualification Requirements including (i) requirements for the qualifications of professional accountants; and (ii) a guideline for national systems for the qualifications of professional qualifications. • Global Curriculum for the Professional Education of Professional Accountants including: (i) organizational and business knowledge; (ii) information technology; and (iii) accounting and accounting-related knowledge. |
|--|--|

Furthermore, ISAR has initiated a project to assess the competence of accountants. The objective of the project is to rate professional accounting qualifications from around the world and, in doing so, create impetus for improvements and support international skill transferability.⁴²

2. Membership Requirements

Education

IFAC and ISAR have published guidelines on education requirements. The IFAC guidelines, such as IEG 9, provide an overview as to what is expected. The ISAR guidelines are more useful in a practical sense as they suggest a detailed curriculum structure and contents.⁴³

Experience

With regards to practical experience, international guidelines state that:

An appropriate period of relevant experience in performing the work of professional accountants must be a component of a pre-qualification program. The period of experience may vary due to differences in the

⁴¹ UNCTAD. 1999. *International Accounting and Reporting Issues: 1999 Review*. United Nations.

⁴² Narayan, Francis B., Ted Godden, Barry Reid, and Maria Rosa Ortega. 2000. *Financial Management and Governance Issues in Selected Developing Member Countries: A Study of Cambodia, People's Republic of China, Mongolia, Pakistan, Papua New Guinea, Uzbekistan, and Viet Nam*. Asian Development Bank. p 29.

⁴³ UNCTAD. 1999. *International Accounting and Reporting Issues: 1999 Review*. United Nations.

environment in which professional accountants offer their services. However, this period should be long enough to permit prospective accountants to demonstrate they have gained the knowledge, skills and professional values sufficient for performing with professional competence and for continuing to grow throughout their careers. This objective cannot normally be met in a period of less than three years.

Paragraph 49—IEG 9.

Moreover, IFAC recommends that practical experience requirements must be considered when professional bodies seek mutual recognition of qualifications.⁴⁴

Continuing Professional Education (CPE)

IFAC and ISAR recommend a minimum of 30 hours CPE per year, or a minimum of 90 hours in every three-year period, of structured learning activity.⁴⁵

3. Quality Control and Assurance

“In the case of professional accountants in public practice, the implementation of appropriate quality control policies and procedures is the responsibility of each firm of practicing accountants. The task of encouraging and assisting firms of practicing accountants to maintain and improve the quality of professional services is primarily that of the member bodies in each country. IFAC believes that the member bodies have the responsibility to take appropriate steps to achieve that objective in the legal, social, business, and regulatory environment prevailing within their countries.”

– IFAC (August 1999)⁴⁶

In relation to quality control and assurance, IFAC suggests that:⁴⁷

- Member bodies should adopt or develop quality control standards and relevant guidance that require firms of practicing accountants to establish the quality control policies and procedures necessary to

⁴⁴ International Federation of Accountants (IFAC). 1995 June. *Statement of Policy of Council: Recognition of Professional Accountancy Qualifications*. New York: IFAC. Paragraph 22-25.

⁴⁵ International Federation of Accountants (IFAC). 1998 May. *International Education Guideline (IEG) 2: Continuing Profession Education*. New York: IFAC.

⁴⁶ International Federation of Accountants (IFAC). 1999 August. *Assuring the Quality of Professional Services*. New York: IFAC.

⁴⁷ International Federation of Accountants (IFAC). 1999 August. *Assuring the Quality of Professional Services*. New York: IFAC.

provide reasonable assurance of conforming with professional standards in performing services. The nature and extent of a firm's quality control policies and procedures depend on a number of factors, such as the size and nature of its practice, its geographic dispersion, its organization, and appropriate cost/benefit considerations. Accordingly, the policies and procedures adopted by individual firms will vary, as will the manner in which the policies and procedures themselves and compliance with them are documented.

- Member bodies should develop quality review programs designed to evaluate whether firms of practicing accountants have established appropriate quality control policies and procedures and are complying with those policies.
- Member bodies should establish quality review programs designed to evaluate whether firms of practicing accountants have complied with relevant professional standards for assurance engagements.
- Member bodies should require firms of practicing accountants to make appropriate improvements in their quality control policies and procedures, or in their compliance with those policies and procedures, when the need for such improvement is identified. Where firms fail to comply with relevant professional standards, the member body should take appropriate corrective action. Member bodies should also take such educational or disciplinary measures as indicated by the circumstances.

As a basic condition, IFAC emphasizes that implementation of an adequate self-regulatory program cannot be effected until firms of practicing accountants in a country are bound by an appropriate code of ethics and also by adequate standards governing accounting principles and engagements to provide professional services. The IFAC *Code of Ethics for Professional Accountants*, its International Standards on Auditing, and the International Accounting Standards (IASs) issued by the International Accounting Standards Board (IASB) all provide guidance for such standards.

Box 2: Professional Quality Assurance in the People's Republic of China

The People's Republic of China provides one example of how a quality assurance program can be implemented.⁴⁸ From July 1997 to March 1999, China conducted a nationwide rectification campaign of the accounting market. The campaign had four stages:

- Self-inspection. In the six months to December 1997, around 6,700 accounting firms conducted self-inspections. The self-inspections covered around 50 percent of their 1996–1997 activities. Just under 1.5 million business reports were inspected; of these, 26 percent were considered to be either defective or in need of correction.
- Focus Groups and Field Inspections. In January 1998, local CPA Institutes established working groups. In the following six months, these working groups conducted field inspections of 5,800 firms.
- Inspection Reviews. From July to the end of October 1998, 192 people selected by the Chinese Institute of Certified Public Accountants (CICPA) reviewed the inspections conducted in stages I and II. The reviews focused on 405 accounting firms.
- Reexamination. From November 1998 to March 1999, CICPA reexamined the qualifications and status of qualified accountants and accounting firms.

As a consequence of the campaign almost 12,700 individual CPAs were either forced to withdraw from the profession or were disciplined (25 percent of CPAs). Many of these were older members who had not passed the uniform accounting examination, and around 580 accounting firms withdrew from the profession or had their licenses cancelled. Warnings and punishments were issued to a further 2,000 accounting firms (43 percent of firms).

CICPA judged the campaign to be a success based on the following evidence.⁴⁹ First, during the period of the campaign, 6,300 newly qualified accountants joined the profession. The net effect was to substantially improve the profession's age structure and knowledge. Second, to address problems that were identified in the inspections, 85 percent of accounting firms substantially improved their internal-management practices; improved professional rules; implemented or improved quality-control systems; increased training; and in doing so, effectively eliminated the problems that had been identified. Third, in 1998, the level of "non-clean" audit opinions given on listed companies rose dramatically (to around 12 percent of audit reports) which (arguably) indicated improved professional quality and ethics. Fourth, the credibility of CPAs in the eyes of the public, as measured by a media survey, climbed from 45 percent in 1996, to 81 percent in June 1998.

⁴⁸ Narayan, Francis, B. and Barry Reid. 2000. *Financial Management and Governance Issues in the People's Republic of China*. Asian Development Bank. pp. 35-39.

⁴⁹ Yong, Li. 1999. The Reform, Regulation and Opening-up of China's Accounting Market. *Contemporary Issues in China Accounting and Finance: Policy and Practice*. Oxford University Press. p. 282-283.

Appendix 8. International Accounting Standards

The following IASs were in effect at 30 September 2001.^{50,51}

| | | | |
|--------|--|--------|---|
| IAS 1 | Presentation of Financial Statements | IAS 27 | Consolidated Financial Statements and Accounting for Investments in Subsidiaries |
| IAS 2 | Inventories | IAS 28 | Accounting for Investments in Associates |
| IAS 7 | Cash Flow Statements | IAS 29 | Financial Reporting in Hyperinflationary Economies |
| IAS 8 | Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies | IAS 30 | Disclosures in the Financial Statements of Banks and Similar Financial Institutions |
| IAS 10 | Events After the Balance Sheet Date | IAS 31 | Financial Reporting of Interests In Joint Ventures |
| IAS 11 | Construction Contracts | IAS 32 | Financial Instruments: Disclosures and Presentation |
| IAS 12 | Income Taxes | IAS 33 | Earnings Per Share |
| IAS 14 | Segment Reporting | IAS 34 | Interim Financial Reporting |
| IAS 15 | Information Reflecting the Effects of Changing Prices | IAS 35 | Discontinuing Operations |
| IAS 16 | Property, Plant and Equipment | IAS 36 | Impairment of Assets |
| IAS 17 | Leases | IAS 37 | Provisions, Contingent Liabilities and Contingent Assets |
| IAS 18 | Revenue | IAS 38 | Intangible Assets |
| IAS 19 | Employee Benefits | IAS 39 | Financial Instruments: Recognition and Measurement |
| IAS 20 | Accounting for Government Grants and Disclosure of Government Assistance | IAS 40 | Investment Property |
| IAS 21 | The Effects of Changes in Foreign Exchange Rates | IAS 41 | Agriculture |
| IAS 22 | Business Combinations | | |
| IAS 23 | Borrowing Costs | | |
| IAS 24 | Related Party Disclosures | | |
| IAS 26 | Accounting and Reporting by Retirement Benefit Plans | | |

⁵⁰ Source: IASC Website: www.iasc.org.uk

⁵¹ The following IASs have been withdrawn:

- IAS 3 was replaced by IAS 27 and IAS 28.
- IAS 4 was replaced by IASs 16, 22, and 38.
- IAS 5 was replaced by IAS 1.
- IAS 6 was replaced by IAS 15.
- IAS 9 was superseded by IAS 38.
- IAS 13 was replaced by IAS 1.
- IAS 25 was replaced by IAS 39 and IAS 40.

Appendix 9. IASB Work Plan

The Work Plan of the International Accounting Standards Board (IASB) as of 30 September 2001 is as follows.⁵²

| Issue | Plan |
|--|--|
| Agriculture | Exposure Draft E65: published July 1999. Final IAS: planned 4th quarter 2000 |
| Business Combinations | Added to Agenda: 4th quarter 1998. G4+1 Discussion Paper: published 2nd half 1998. Specific IASC steps are not yet determined. |
| Business Reporting on the Internet | Staff Research Project. Discussion Paper: published November 1999. Added to the Board's Work Program: March 2000. |
| Emerging Economies | Project Added to Agenda April 1998. August 2000: Survey on Barter Transactions. |
| Extractive Industries (including Mining and Oil and Gas) | Project Added to Agenda April 1998. Issues Paper: planned 3rd quarter 2000. |
| Financial Instruments—Comprehensive Project | Issues Paper: published 1st quarter 1997. Joint Working Group Report including draft Exposure Draft: planned 2000. |
| Financial Instruments—Recognition and Measurement | Final IAS 39: published December 1998. Exposure Draft E66, Limited Revisions to IAS 39: published July 2000. Implementation guidance is being developed. |
| Insurance | Project approved April 1997. Issues Paper: published December 1999. |
| Pension Plan Assets | Exposure Draft E67: published July 2000. |
| Present Value (formerly 'Discounting') | Project Added to Agenda April 1998. Issues Paper: planned 2nd half 2000. |
| Reporting Financial Performance | G4+1 Position Paper: published August 1999. Draft Statement of Principles: planned 4 th quarter 2000 |

⁵² Source: IASC Website. http://www.iasc.org.uk/frame/cen3_4.htm

APPENDIXES

| Issue | Plan |
|---|---|
| Disclosures by Banks and Similar Financial Institutions | Steering Committee appointed: June 2000 |
| Tax Consequences of Dividends | Exposure Draft ED 68: published July 2000 |
| Transition | Undecided |

Appendix 11: International Standards and Guidance on Accountancy Education

International organizations have issued guidance on accountancy education issues. This guidance includes:

- *Quality Issues For Internet and Distributed Learning in Accounting Education.* This International Federation of Accountants (IFAC) Education Committee discussion paper discusses the environment that encourages the design, development and delivery of high-quality Internet and distributed learning in global accounting education. It offers recommendations for assessing the quality of Internet education and distributed learning.⁵³
- *Discussion Paper on Assistance Projects in Accountancy Education and Development.* This IFAC Education Committee discussion paper, which is based on the experiences of 15 IFAC member organizations, looks at some of the common aspects of successful aid and assistance projects and the impediments that can derail the process. It is meant to be of assistance to accountancy organizations and consultants involved in aid projects for the development of accountancy education, as well as potential donors.⁵⁴
- *International Education Guideline 9: Accounting Education and Experience.* This IFAC guideline sets out high-level curriculum expectations.⁵⁵
- *Guideline for a Global Accounting Curriculum and Other Qualification Requirements.* This United Nations Conference on Trade and Development (UNCTAD) report sets out (i) requirements for the qualifications of professional accountants; and (ii) a guideline for national systems for the qualifications of professional qualifications.⁵⁶

⁵³ International Federation of Accountants (IFAC). 2000. *Quality Issues For Internet and Distributed Learning in Accounting Education*. New York: IFAC Education Committee. www.ifac.org

⁵⁴ International Federation of Accountants (IFAC). 2000. *Discussion Paper on Assistance Projects in Accountancy Education and Development*. New York: IFAC Education Committee. www.ifac.org

⁵⁵ International Federation of Accountants (IFAC). 1996. *Guideline 9: Accounting Education and Experience*. New York: IFAC.

⁵⁶ UNCTAD. 1999. *International Accounting and Reporting Issues: 1999 Review*. United Nations.

- *Global Curriculum for the Professional Education of Professional Accountants.* This UNCTAD report sets out curriculum requirements including: (i) organizational and business knowledge; (ii) information technology; and (iii) accounting and accounting-related knowledge.⁵⁷

⁵⁷ UNCTAD. 1999. *International Accounting and Reporting Issues: 1999 Review*. United Nations.

Appendix 12: Auditing Services Law 1995

This law concerns the establishment of auditing services in the Azerbaijan Republic, the legal grounds for its realization, determines auditor's functions, legal rights and duties, envisages the creation of an independent financial control system for protection of owners' right of property.

Relations connected with the auditing services are regulated by the present law, as well as by other legislative acts of the Azerbaijan Republic, by international agreements and contracts

CHAPTER I—GENERAL PROVISIONS

Clause 1. Sphere of the Law's Application

The present law is applicable to all enterprises, organizations and institutions (further called "economic subjects") functioning on the territory of the Azerbaijan Republic irrespective of kind of their property and of their organizational and legal subordination.

Clause 2. The Term "Audit"

The term audit means independent examination of accounts and financial reports of economic subjects engaged in producing and dealing with goods, rendering services and fulfilling works, to check that the said accounts and reports are exact and correct.

The audit can be done compulsorily or voluntarily (initiated by the economic subject itself). According to legislation the audit is compulsory for the economic subjects that are obliged to publish their accounts, as well as in the cases specified by legislative acts or in accordance with a corresponding decision of an authorized state body, and is voluntary in all other cases.

Clause 3. Auditing Services

Auditing services consist of carrying out on a basis of a contract the examination, expert investigation, analysis, submission of a written report about the financial-economic activity of economic subjects, including the assistance in accounting, confirmation of exactness of reports figures, rendering other services in the field of professional activity of the auditor (in accordance with the charter of the audit company).

The audit services do not exclude the examination of the economic subject's activity by the state bodies of their own accord.

Clause 4. Independent Auditor

The independent auditor is a natural person who has been granted a license to render auditing services on the territory of the Azerbaijan Republic by the Audit Chamber of the Azerbaijan Republic (called further "Audit Chamber").

Clause 5. Audit Company

The audit company is a legal entity rendering the auditing services in accordance with its charter on the territory of the Azerbaijan Republic on a basis of the license granted to it by the Audit Chamber.

To establish an audit company at least three independent auditors are needed.

Clause 6. Requirements Demanded from the Independent Auditors

The following is required to be an independent auditor in the Azerbaijan Republic:

- 1) to be a citizen of the Azerbaijan Republic;
- 2) a valid court's decision about canceling a previous restriction to take certain

positions in the field of financial-economic relations or be engaged in certain activities, or about acquittal of any charges connected with such activities;

3) to have higher education in the field of accounting, finance, economic and legal disciplines, and at least three years of working experience in one's specialty;

4) to pass the auditor examination.

Persons convicted for crimes committed by mercenary (self-interest) reasons and not acquitted cannot be auditors.

A foreign citizen having the auditor license of his own country through official permission of the Audit Chamber can use his right to render auditing services on the territory of the Azerbaijan Republic.

Clause 7. Examination in order to get the auditor rank

To take examinations for granting the auditor rank the Audit Chamber establishes a special commission.

The examinations are carried out in an order prescribed in the charter of the Audit Chamber.

Clause 8. Auditor's report

The auditor's report certified by his (audit company's) signature and stamp (seal) represents for all legal and natural persons, government, executive and legislative bodies, as well as for courts an official and legal document testifying the financial position of the audited economic subject, the exactness of its annual accounting documents, and the estimation of the general situation with its business accounts.

The auditor's report reflecting the results of examination carried out on a basis of the authorized state body's decision is considered equivalent to the report of the expertise carried out in accordance with the legislation of the Azerbaijan Republic.

The general form and requirements to composition of the auditor's report are determined by the Audit Chamber.

CHAPTER II. REGULATION OF THE AUDITING SERVICES IN THE AZERBAIJAN REPUBLIC

Clause 9. Auditing services regulation

In order to establish the state regulation of auditing services; to prepare norms, acts and measures aimed at the improvement of the auditing services in the Azerbaijan Republic; to protect interests of the state, of economic subjects and of auditors (audit companies), to see that all legal demands are properly observed in the course of the auditor's (audit company's) activity, the Audit Chamber of the Azerbaijan Republic is being established. The activity of the Audit Chamber is governed by its Charter.

The Supreme Council of the Azerbaijan Republic approves the Charter of the Audit Chamber and appoints its head.

Clause 10. License to implement auditing services

Independent auditors and audit companies can function on a basis of a license that is valid for five (5) years.

Clause 11. Registration of independent auditors and audit companies

The auditor acquires the right to render auditing services from the date of issuing the license for such activity to him and entering his name in the register of auditors.

The auditor can carry out his activity independently or as a member of an audit company. He is forbidden to be engaged in any other activity.

The independent auditors must keep a journal registering their activities. They must submit this journal to the Audit Chamber for checking their activities and for controlling the quality of auditing services.

The Audit Chamber implements the registration of auditors and audit companies on the territory of the Azerbaijan Republic.

The audit company consisting of not less than three auditors after having acquired a license for auditing services and been registered at the Audit Chamber has a right to render the auditing services.

CHAPTER III. AUDITOR'S RIGHTS, DUTIES AND RESPONSIBILITY

Clause 12. Auditor's rights

The independent auditor and audit company have the following rights:

- to determine independently the form and methods of the audit in accordance with the requirements of the present law and of the agreement concluded with the customer;
- to acquaint himself with all documents (including those kept by other legal persons) relevant to the financial and economic activity of the customer and to take them for examination, to check the available cash, securities, valuables, to get all information needed for the auditing work;
- to get written explanations from the customer's management and employees;
- while carrying out the auditing work by an order of authorized state bodies to bring up questions for their consideration about revealed violations and defects;
- to invite other auditors to the auditing work on a basis of agreements;
- to refuse to carry out the audit if the economic subject fails to submit documents which are necessary for the audit.

Clause 13. Auditor's duties

The independent auditor's and audit company's duties consist of the following:

- strict observance the requirements of legislation of the Azerbaijan Republic during the implementation of auditing services;
- to implement the audit examination and other auditing services with good quality;
- to inform immediately the customer (authorized state body) of the impossibility to participate in audit due to circumstances specified in Clause 18 of the law;
- to check as thoroughly as possible the compliance of the customer's accounts and reports with existing laws and normative acts;
- to inform the customer's management of all violations, errors in the accounting and reporting documentation discovered in the course of audit;
- to keep in strict confidence (except by demand from the law court) the information obtained during the audit initiated by the customer;
- to guarantee the safe preservation of documents which have been acquired or prepared during the examination;
- to give the economic subject by his demand detailed information about legal requirements concerning the audit, about the parties' rights and duties, as well as about normative acts concerning the defects and consequences described in the auditor's report.

Clause 14. Auditors' responsibility

If auditors or audit company fail to fulfill their duties in accordance with requirements of the legislation of the Azerbaijan Republic and of the agreement concluded with the customer they can bear property responsibility for that.

Clause 15. Withdrawal of the license to implement auditing services

The license granted to the auditor or to the audit company to carry out audit activity on the territory of the Azerbaijan Republic can be withdrawn on a basis of the Audit Chamber's decision in the following cases:

- in case of three unsuccessful audits during one calendar year;
- if in the course of audit the requirements of the present law and of the legislation of the Azerbaijan Republic were seriously violated;
- if the court's decision comes into legal force depriving the independent auditor of his right to take certain position in the field of financial-economic relations, or be engaged in certain activities, or imposing a penalty for crimes committed for self-interest reasons;
- if after the issuance of the license it was discovered that the applicant had given false information in order to get the license;
- except the cases specified by legislation, if the auditor has transferred the information obtained in the course of the audit to the third parties without the consent (permission) of the head (owner) of the economic subject;
- if the auditor (audit company) has concealed the circumstances specified in Clause 18 of the present law which prevent him from fulfilling the audit.

CHAPTER IV. GENERAL RULES OF THE AUDIT SERVICE RENDERING IN THE AZERBAIJAN REPUBLIC

Clause 16. Organization of auditing services at the economic subjects

The auditing servicing can be rendered on a basis of an agreement concluded between the independent auditor or audit company, on the one hand, and the customer, on the

other hand; the said agreement must specify the examination purposes, its duration, volume of consulting services, the expenses and procedure for their payment, as well as responsibility of the parties.

The customer is obliged to create all necessary conditions for the auditor to carry out his professional duties in full extent and with good quality.

The auditor is independent of his customer or of any other third person interested in this work.

The fulfillment of the agreement's requirements by the auditor or audit company is certified by an acceptance certificate of the auditor's report. The auditor's report must be written in accordance with specified requirements.

Clause 17. Rights and duties of the economic subject in connection with auditing services

The management (owner) of the economic subject is obliged to submit to the auditor all documents, registers and reports needed for the audit and bears responsibility for their correctness. He is obliged to give the auditor by his demand written and verbal explanations.

The economic subjects can freely choose the auditor.

The economic subjects have a right to conclude agreements for any period with the independent auditor or audit company on all issues connected with financial-economic activities. The auditor prepares a report in the prescribed form on the results of the investigation fulfilled according to such agreement.

CHAPTER V. SPECIAL PROVISIONS

Clause 18. Audit services restrictions

Auditors cannot audit the enterprises where they have personal property

interests, or have kindred with any of its managing persons, are its founders, owners or shareholders, or previously rendered to it their professional services.

Clause 19. Dispute settlement

All property disputes arising between the auditor (audit company) and his customers, if they cannot be settled by the Audit Chamber, must be settled by court (arbitration court).

The auditor (audit company) can apply in the prescribed order to a law court (arbitration court) if the Audit Chamber

has refused to grant him a license or has withdrawn it, or has refused to register the audit company as a legal person.

Clause 20. Inspection of the audit company

The Audit Chamber inspects the compliance of the audit company's activity with the requirements of the present law, and supervises its activity.

RATIFIED by the resolution of National Council of Azerbaijan Republic, Baku, September 19, 1995 N 1115

Appendix 13: Provisions of the Chamber of Auditors of Azerbaijan

I. GENERAL CLAUSES

1. Chamber of Auditors of Azerbaijan Republic (further “Chamber”) is an independent financial body, carrying out the organization of the state policy and development of audit services, protection of the properties of the owners, State interests, subjects leading their economy and auditors, supervision of the observance of requirements by independent auditors and audit organizations in their activity; any such requirements arising from the legislative Acts of the Republic.

2. In its own activity the Chamber is governed by the Law of Azerbaijan Republic “On audit service”, by the present provisions, and also by other normative Acts.

3. The Chamber is a legal entity, with settling, currency and special accounts in the bank. It has round stamp with the picture of State Emblem of Azerbaijan Republic on it and with its name, and other stamps.

4. Audit services are paid on the basis of contracts concluded between independent auditors and registered audit organizations, and between the enterprises and organizations, but under contracts by legal and other bodies for conducting of revisions and inspections on the enterprises and in the organizations – by mentioned bodies in the according order

5. Place of the Chamber location - Baku

II. OBJECTIVES AND FUNCTIONS OF THE CHAMBER

6. The principal function of the Chamber is the organization of work of audit service in the Republic and carrying out the measures on development and improvement of its activity according to Legislation for ensuring

precise and authentic policy of financing and accounting and calculation in all the subjects leading their economy irrespective of forms of ownership.

7. The Chamber fulfill the following functions:

- organizes and adjusts the work of audit service in Azerbaijan Republic; grants in the territory of Azerbaijan Republic the License to the independent auditors and audit organizations, carrying out supervision at their work and in the accordance to the Charters of audit organizations according to the Law of Azerbaijan Republic “On audit service”;
- carries out the registration, account of the independent auditors and audit organizations and grants the certificates to them on registration;
- works out and ratifies the rules of exams on granting of licenses, giving rights to deal with the audit activity in the territory of Azerbaijan Republic;
- prepares and ratifies composition and provision of examination commission on granting of licenses, giving right to deal with audit activity, fixes the payment for examination;
- prepares and ratifies forms of audit conclusions on financial and accountant reports of subjects leading their economy, various reports about the independent auditors and audit organizations;
- consults the independent auditors and audit organizations on matters of audit experience summery and application of acting legislative acts, prepares proposals on development and improvement of audit service and carries out the supervision for their realization;

- prepares instructions, recommendations and methodical indications on conducting the audit;
- makes up normative documents about forms and methods of rendering services, prepares proper recommendations on the basis of permanent study of national and international experience;
- provides the consideration according to the legislative acts of the republic, the claims of customers to the independent auditors and audit organizations for non-fulfillment of their proper professional duties;
- Carries proper measures on protection of rights and legal interests of the independent auditors and audit organizations;
- Verifies that financial-economic activities of independent foreign Auditor and subsidiary and/or agencies of foreign audit organizations conform with the Law on "Audit service in the Azerbaijan Republic" and controls their work;
- Carries the repeated audit;
- Makes audit conclusions on authenticity of economic subjects' property evaluation with respect to privatization of the state enterprises and other purposes. (Supplemented by the decree of the National Assembly of the Azerbaijan Republic dated March 12, 1996 with changes and supplements in Regulations of the Chamber of Auditors of the Azerbaijan Republic).
- to receive from the independent auditors and audit organizations reports in fixed form;
- to give to the auditors and audit organizations instructions and methodical indications obligatory to fulfillment;
- to consider disputes between the independent auditors and audit organizations and between the customers;
- to consider and settle complaints against acts of the auditor;
- to adjust business ties with international organizations dealing with audit activity, and to present in foreign countries the interests of Azerbaijan Republic on audit items;
- to prepare and improve audit employees;
- to settle other matters of audit service within the competency of the Chamber;
- to render services to legal entities and persons with respect to audit activity and financial-economic relations;
- to render audit services on the basis of contracts with economic subjects;
- to set up audit organizations. (supplemented by the decree of the National Assembly of the Azerbaijan Republic dated March 12, 1996 with changes and supplements in Regulations of the Chamber of Auditors of the Azerbaijan Republic).

III. AUTHORIZATIONS OF THE CHAMBER

8. The Chamber has the following authorizations:

- to examine quality of audit of the independent auditors and audit organizations, and if there is violation of the law, to revoke the license for audit activity;

IV. MANAGEMENT BY CHAMBER

9. The Chairman of Chamber and his deputy are appointed by the Supreme Council of Azerbaijan Republic. They are authorized by leaders of central state executive bodies fixed by legislation of Azerbaijan Republic.

10. The Chamber is managed by its Chairman. He bears personal responsibility for the execution of tasks and liabilities

laid down by the Chamber and the realization of its functions.

11. Structure, staffs, salary of employees and estimates of Chambers expenditures within its own means are ratified by the Chamber Chairman. The Chairman of the Chamber in accordance with the labor law hires and dismisses its employees, encourages them and imposes upon them penalties.

12. To conduct service functions there is a management body, a Council is set up in the Chamber. The composition of the Council comprises the Chairman of the Chamber, a deputy, leaders of two leading departments, one representative from audit organizations, independent auditors and Minister for finance of Azerbaijan Republic.

13. The Chairman of the Chamber declares the Members of the Council.

14. The meetings of the Council are held not less than one time per quarter.

V. ORGANIZATION OF EXAMS TO OBTAIN AUDITOR'S TITLE

15. Examination for the title of auditor is conducted by an exam commission appointed by the Chamber (further - "commission").

16. The composition of the commission comprises three representatives of Chamber of Auditors, one representative from Ministry of finance, head of state tax inspection, National Bank, scientist-economists, independent auditors and audit organizations. At the beginning of each year the composition of the commission is declared by the Chairman of the Chamber.

17. The members of the Commission are to have great experience in the field of audit service with not less than 10 years of practical work on one of specialties of accountant calculation, finances, economy and law.

18. Salary of commission members is fixed.

VI. PROPERTY OF THE CHAMBER

19. Property (income) of the Chamber is raised from: payments for passing the exams and granting licenses; incomes from registration of audit organizations; members fees of independent auditors and audit organizations (including foreign, legal and physical persons); sums paid for rendering audit services on contracts; other resources not prohibited by Legislation; receipts from sales issued on the matters of audit instructions and methodical indications, books, newspapers and magazines and incomes from any authorized activity.

20. Property (or income) of the Chamber is available for its disposal and circulation.

21. Income after payment of duties stipulated by Legislation, is to be disposed by the Chamber according to the purpose they were raised.

22. The procedure for formation and utilization of funds is ratified by the Council of the Chamber.

VII. MEMBERS OF THE CHAMBER

23. Independent auditors and audit organizations are qualified to be Members of the Chamber.

24. Members of the Chamber are to pay membership fees in fixed order.

25. Amount of fee is established by the Council and is according to the account of expenditures of the payers.

VIII. ACCOUNTING CALCULATION AND REPORT (ACCOUNT)

26. The Chamber in fixed order presents to the tax and statistical bodies in the territory of their allocation summaries of their own activity on accounting and statistical account.

Appendix 14: Law on Banking 1996

The Law of the Azerbaijan Republic on banks and banking activity (Law No . 123-IT Baku, July 14, 1996).

CHAPTER I. GENERAL PROVISIONS

CHAPTER II. LICENSING OF BANKING ACTIVITY

CHAPTER III. OWNERSHIP AND MANAGEMENT OF BANKS

Article 24. Finance-auditing committee

1. Finance-auditing committee is elected by the general meeting for the period not exceeding four years. It is composed of odd number of members, but not less than three. Members of Supervisory Council and the board are not entitled to serve at the same time as the members of finance-revision committee. The general meeting elects the chairman of the committee. Finance-revision committee: (i) controls the execution of banking legislation, normative acts of the National Bank and the Articles of credit organization; and (ii) fulfils accounting control.

2. Finance-revision committee executes audits according to the plan it adopts and by the demand of the Supervisory Council, the board and shareholders, representing over 10 percent of votes and in other cases, specified by the Articles. The general meeting does not have the right to approve the annual balance without the statement of finance-revision committee.

3. Committee resolutions are adopted with a simple majority of votes. Abstention from voting is prohibited.

4. The general meeting is entitled to award the members of the committee; awards are to be granted only from the net profit of credit organization.

CHAPTER IV. BANKING ACTIVITY

CHAPTER V. RELATIONS BETWEEN CREDIT ORGANIZATIONS. RELATIONS OF CREDIT ORGANIZATIONS WITH CLIENTS

CHAPTER VI. SAVINGS SPHERE

CHAPTER VII. RESPONSIBILITY FOR INFRINGEMENT OF BANKING LEGISLATION

CHAPTER VIII. CONSERVATION AND LIQUIDATION

CHAPTER IX. ACCOUNTING AND REPORTING OF CREDIT ORGANIZATIONS. CONTROL OVER ITS ACTIVITY

Article 49. Accounting and Reporting

1. Regulations of accounting in credit organization, the character, volume and terms for submitting of its reports are fixed by the National Bank.

2. Accounts, reporting documentation and financial accounting of credit organization are to reflect operations and financial state of its branches. During the annual report the credit organization is to submit summarized balance and report of profits/ losses with consideration of the report of affiliated credit organizations.

3. Branches of foreign banks are to submit their reports to the National Bank in compliance with the requirements of the present article.

Article 50. Audit of Credit Organization

Finance-economic activity of credit organization is subject to annual audit by auditors who are selected by the organization itself or if necessary, appointed by the National Bank. After the notification of the National Bank of audit results, the annual balance and report of profits/losses are published in papers in the form and within terms, established by the National Bank.

Article 51. Reporting and Inspections

1. Credit organization prepares report of administrative control and conducted operations, its liquidity-credit capability and profitability. Reports are made in the

form and with details, established by the normative acts of the National Bank and are periodically submitted to the National Bank. Reports are submitted to the general meeting of shareholders.

2. Audits of credit organizations and their branches are executed only by the National Bank in the order, specified by the article 50 of the present Law, excluding audits, made by the State Tax Inspectorate of the Azerbaijan Republic. If other bodies of state power conducting audits and control functions, provide the National Bank with the motivated applications, the National Bank is entitled to carry out the audit itself or invites an auditing organization.

Appendix 15: Law on Enterprises 1994

Relevant Extracts.

CHAPTER I. GENERAL PROVISIONS

CHAPTER II. TYPES AND ORGANIZATIONAL AND LEGAL FORMS OF ENTERPRISES

Clause 4. Types of Enterprises

According to the Law of the Azerbaijan Republic "On property in the Azerbaijan Republic" can refer to enterprises based on state, collective, private and mixed kinds of property.

Clause 5. Organizational and Legal Forms of Enterprises

Enterprises function in the organizational and legal forms of a state enterprise, individual (family) enterprise, general partnership, limited partnership, limited liability enterprise and joint stock company.

Clause 6. State Enterprise

There are the following forms of the enterprises based on state property:

enterprise, property of which is in full state ownership;

enterprise, the controlling block of shares of which is owned by state bodies.

The state-owned enterprise in compliance with legislation of the Azerbaijan Republic is established by state bodies authorized to manage the state property.

Clause 7. Individual (family) Enterprise

Clause 8. General Partnership

Clause 9. Limited Partnership

Clause 10. Limited Liability Enterprise

Clause 11. Joint Stock Company

Clause 12. Association of Enterprises

CHAPTER III. ESTABLISHMENT, LIQUIDATION AND REORGANIZATION OF ENTERPRISES

CHAPTER IV. STATE AND ENTERPRISE

CHAPTER V. PROPERTY OF THE ENTERPRISE

Clause 30. Financial and Auditing Commission of the Enterprise

In order to control and audit the financial and economic activity of the enterprise a financial auditing commission is established.

The member of the financial auditing commission cannot be a member of the management or the supervisory council of the enterprise.

The financial-auditing commission audits the economic and financial activity of the enterprise in the following cases:

- a) on completion of the economic year;
- b) on demand from the general meeting;
- c) on demand from members of the supervisory council and management;
- d) in other cases envisaged by the charter.

CHAPTER VII. ECONOMIC AND SOCIAL ACTIVITY OF THE ENTERPRISE

Clause 38. Accounting and Reports of the Enterprise

In accordance with the results of its activity the enterprise keeps operational and accounting records, statistical reports.

Forms of the state statistical reports are determined by the state statistics bodies and include only actual data, addresses and terms of submission of the information. The information not envisaged by the state statistical accounting can be submitted by the enterprise only on a basis of an agreement or in the case and by a procedure determined by legislation of the Azerbaijan Republic.

Officials of the enterprise are responsible for distortion of the state accounting as specified by legislation.

CHAPTER VIII. LIABILITY OF THE ENTERPRISE AND CONTROL OVER ITS ACTIVITY

Clause 40. Liability of the Enterprise

For violation of agreement obligations, credit, accounting and taxation procedures, requirements to production quality, other

rules of implementing of the economic activity the enterprise has property accountability (liability) as specified by the relevant legislation of the Azerbaijan Republic.

Clause 41. Control over the Enterprise's Activity

All-round (complex) auditing of the financial-economic activity of the enterprise is carried out by the owner's initiative at least once every year.

Taxation and other state bodies that are authorized by legislative acts of the Azerbaijan Republic to check various aspects of the enterprise's activity, if needed can carry out inspection within the limits of their power (authorization). The enterprise has a right not to meet demands of such bodies on matters not in their competence, or not connected with such inspection.

Appendix 16: Law on Joint Stock Companies 1994

Relevant Extracts.

CHAPTER I. GENERAL PROVISIONS

CHAPTER II. ESTABLISHMENT OF A COMPANY

CHAPTER III. SHAREHOLDERS' POWERS AND DUTIES

Article 15. Auditing the Company's Activity by a Shareholder's Demand

1. The shareholder(s) who own not less than one-tenth of the company's registered funds can demand from the supervisory council to audit the enterprising activity of the company, indicating his (their) purposes and reasons for it.

2. In case the supervisory council fails to fulfill within 30 days this demand, described in subclause 1 of this article, the shareholders can apply to the general meeting.

3. If the general meeting fails to meet the shareholders' demand the latter(s) can apply to court.

CHAPTER IV. FUNDS AND PROPERTY OF THE COMPANY

CHAPTER V. MANAGEMENT OF THE COMPANY

Article 21. Company General Meeting

1. The general meeting of shareholders (founders) represents the suprememanaging body of the company.

The exclusive competence of the general meeting embraces:

- to determine the main directions of the company's activity, to approve the prepared plans and reports;

- to make changes in the articles of association of the company;

- to elect and recall the personnel of the supervisory council, management and control financial-auditing commission;

- to approve the results of work during the year (including that of subsidiaries), reports of the control and financial auditing commission;

- to establish branches (subsidiaries) and representations, to approve their articles of association and their liquidation;

- to make decisions about calling the company's officials to property accountability;

- to approve the organizational structure and routine of the company;

- to fix salaries for the officials of the company, its subsidiaries, and to cease activity of the company.

The general meeting is considered competent if it is attended by not less than 60 percent of the shareholders having the voting right.

The following matters can be solved by a majority of the shareholders present at the general meeting:

- alteration of the articles of association of the company;

- cessation of activity of the company;

- establishment and liquidation of subsidiaries.

- All other matters can be settled by a simple majority of the shareholders present at the general meeting.

5. The general meeting must be held once in a year unless otherwise specified by the articles of association.

6. An extraordinary general meeting in order to guarantee the interests of the shareholders is summoned by the management, supervisory council and financial-auditing commission.

Article 24. Financial Auditing Commission of the Company

1. The financial-auditing commission is established in order to control (check) and audit the economical and financial activity of the company. Members of the financial-auditing commission are elected by the general meeting.

2. The financial-auditing commission monitors the financial and economic activity of the company. The financial-

auditing commission makes up its report based on the annual account and balance. Without such report (conclusion) of the financial auditing commission the general meeting of the shareholders cannot approve the annual account.

3. The financial-auditing commission carries out the auditing of the financial and economic activity of the company in the following cases: on completion of the economic year; on demand from the general meeting of the shareholders; on demand from the shareholders who own one-tenth of vote; on demand from the supervisory council and management; or in other cases specified by the articles of association.

CHAPTER VI. LIABILITIES OF THE COMPANY AND CESSATION OF ACTIVITY