

# **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.<sup>1</sup>

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

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<sup>1</sup> 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

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**T**he 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

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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

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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

IFRS	International Financial Reporting Standard <sup>2</sup>
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

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<sup>2</sup> 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).

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

**A**zerbaijan 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 Reponses

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 reports 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.