

ASIAN DEVELOPMENT BANK

TAR: MON 36242

TECHNICAL ASSISTANCE

TO

MONGOLIA

FOR

**CAPACITY BUILDING FOR ACCOUNTING
AND AUDITING PROFESSIONALS**

September 2002

CURRENCY EQUIVALENTS

(as of 14 August 2002)

Currency Unit	–	Togrog (NMT)
NMT1.00	=	\$0.00090
\$1.00	=	NMT1,111

ABBREVIATIONS

ADB	–	Asian Development Bank
CPA	–	certified public accountant
CPE	–	continuing professional education
GRP	–	Governance Reform Program
IAS	–	international accounting standards
IFAC	–	International Federation of Accountants
ISA	–	international standards on auditing
MICPA	–	Mongolian Institute of Certified Public Accountants
MOFE	–	Ministry of Finance and Economy
TA	–	technical assistance

NOTE

In this report, "\$" refers to US dollars.

I. INTRODUCTION

1. During the 2002-2004 Country Strategy and Program Review, the Government of Mongolia requested Asian Development Bank (ADB) assistance to strengthen the country's accounting and auditing systems and expedite their implementation in accordance with international standards.¹ In 2000, as part of a regional technical assistance (TA),² ADB conducted a diagnostic study of accounting and auditing arrangements in Mongolia. The recommendation of the study and the experience gained from implementing the Governance Reform Program (GRP) underscore the need to further strengthen accounting and auditing arrangements to support broader economic reforms. Improvements in financial management are critical components of the Government's long-term GRP,³ which ADB has supported through a program loan and an associated TA.

II. ISSUES

2. In the former centrally planned economy, state agencies in Mongolia were the primary users of accounting and auditing system informations. The primary function of accounting was to monitor and control the use of economic resources to meet planned targets, and auditing was limited to an inspection function. As such, the 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 given. Since enterprises were wholly state-owned and their creditors were also the other state-owned enterprises (SOEs), the need for independent financial reporting and control was not recognized. Mongolia followed for many years the Soviet accounting model, which neither met international standards nor catered to the needs of investors or lenders. In addition, the users of financial information were unfamiliar with what they should demand from organizations.

3. During its transition to a market economy, Mongolia has opened several sectors of its economy to domestic and foreign private investment. The Government's policy is to mobilize its financial resources effectively through rational savings and investment decisions that need comprehensive, timely, and transparent financial information from both public and private sectors. These measures represent an integral part of the country's public and financial sector reforms and promote a core component of ADB's strategic development objective for the country.

4. In the public sector, the responsibility for maintaining accounting systems and reporting financial results lies with budget entities. Budget entities are responsible for their own budget control, financial management, accounting, and reporting under the authority of the budget act and instructions issued by the Ministry of Finance and Economy (MOFE). The law requires budget entities to produce accrual-based financial statements in accordance with international public sector accounting standards. Generally each budget entity has a chief accountant directly responsible to MOFE, particularly to the treasury. A regulation passed in June 2001 provided MOFE powers to appoint, dismiss, and qualify chief accountants at budget entities. This is the first step in mobilizing a more unified and effective approach to the appointment of accountants in the Government sector. Audits conducted in the public sector are in the nature of inspections that aim to conduct detailed examination to discover instances of noncompliance with regulations. The integrity of financial statements is questionable, as audits do not include an

¹ The TA first appeared in ADB Business Opportunities in August 2002.

² ADB, 1999. *Technical Assistance for Strengthening Financial Management and Governance in Selected Developing Member Countries*. Manila.

³ ADB, 1999. *Report and Recommendation of the President to the Board on a Proposed Loan to Mongolia for the Governance Reform Program*. Manila.

opinion on the reliability of the financial statements nor conduct performance audits of the integrity of financial statements. To address these issues, the Government plans to establish the legal authority for such audits.

5. The Government also recognized the inadequacies of its existing accounting and auditing systems for the private sector and has decided to promote internationally recognized standards. To support this objective, the Government promulgated the Accounting Law in 1993 (amended in 2001), which mandates business enterprises to adopt international accounting standards (IAS) and submit their audited quarterly financial statements to MOFE. The law required the establishment of the National Association of Certified Public Accountants, which was upgraded to the Mongolian Institute of Certified Public Accountants (MICPA) in 1996. Also, the Auditing Law introduced in 1997 required the adoption of international standards of auditing (ISA).

6. The main obstacles in adopting IAS are (i) accountants' lack of adequate knowledge and experience; (ii) insufficient number of qualified accounting professors and lecturers; and (iii) lack of accounting formats, manuals, and instruction materials that can be used by accountants. Furthermore the limited number of qualified accountants posed difficulty in fully adopting the IAS. Mongolia's accountancy and auditing profession need to encourage a greater degree of awareness of the significance of compliance with international standards in accounting and auditing and develop capacities to support effective enforcement of legislation.

7. Although the Auditing Law 1997 requires auditors to apply ISA, there is still major noncompliance due to (i) auditors' lack of required knowledge in applying ISA, and (ii) incomplete translation of ISA.

8. While the legislative framework for the accountancy and auditing profession is sound, there is need for a fully functioning and competent profession. Strengthening training and teaching capacity is critical to support the planned reforms in public sector financial management and promote efficient private enterprises. MICPA, the professional accountancy body, is confronted with the challenge of improving the regulatory system and the capacity to address the existing weaknesses of the accountancy profession through (i) reforms in the certified public accountant (CPA) examination to ensure that new entrants to the profession will be more qualified; (ii) development of a sustainable and compulsory continuing professional education (CPE) program for CPAs; and (iii) implementation of effective training programs to build the capacities of accountants and auditors.

9. The Government has pursued accounting reforms that have been jointly supported by a few aid agencies. An ADB TA⁴ in 1995 supported the drafting of the law on accounting and auditing as well as the constitution and by-laws of MICPA.⁵ To sustain the momentum of this process, a second TA⁶ was provided in 1997.⁷ The TA helped (i) 18 accountants to qualify in the first CPA examination conducted in accordance with international standards; (ii) 100 accountants to train in IAS in general and a further 36 accountants to train in IAS applicable to banks and financial institutions; (iii) MICPA develop a new syllabus for CPA examinations. MICPA now conducts, supervises using global professional standards, and evaluates independently the CPA examination results; and (iv) MICPA's admission to the Confederation of Asian and Pacific Accountants. Both TAs were rated successful in the technical assistance

⁴ ADB. 1995. *Technical Assistance to Mongolia for Improving Accounting and Auditing Systems*. Manila.

⁵ ADB. 1998. *Technical Assistance Completion Report on Improving Accounting and Auditing Systems in Mongolia*. Manila.

⁶ ADB. 1997. *Technical Assistance to Mongolia for Improving Accounting and Auditing Systems 2*. Manila.

⁷ ADB. 2001. *Technical Assistance Completion Report on Improving Accounting and Auditing Systems in Mongolia*. Manila.

completion report. In addition, the Accounting Development Project in 1993 and 1994 of the World Bank facilitated accounting education and adoption of IAS by SOEs. The United Nations Development Programme provided assistance in developing and delivering a training program to finance staff in government organizations.⁸

10. As part of a regional TA in 2000, ADB conducted a diagnostic study of accounting and auditing arrangements in Mongolia (footnote 2). The study conducted in consultation with representatives of Government, private sector, and international organizations reviewed (i) accounting and auditing standards, (ii) professional infrastructure, (iii) accounting and auditing training, (iv) Government budgeting and accounting, and (v) efficacy of external assistance. The study identified deficiencies in those arrangements and made recommendations to strengthen the profession.

11. The proposed TA will build on the past work of ADB and other external agencies and draws on recommendations of ADB's diagnostic study. The TA will focus on a group of public and private enterprises to convert their accounting system into IAS, as well as improve the capacity of practicing Mongolian accountants and auditors. The upgrading of enterprises to IAS along with training accountants and auditors will help Mongolia align its accounting and auditing arrangements with international standards. The TA framework is in Appendix 1.

12. The development of the accounting and auditing profession is a long-term task that requires continued assistance. The TA objectives are in line with one of ADB's core strategic areas of intervention to promote good governance. It is also in conformity with the crosscutting strategic theme of promoting the role of the private sector in development and ADB's anticorruption policy.⁹ Strengthening accounting and auditing practices will have a direct effect on the efficient management of enterprises. It will also contribute to enterprise reforms that ADB has been supporting. Improving financial management and strengthening audit functions are some measures that will lead to accountability and transparency, which are features of sound development management.

III. THE TECHNICAL ASSISTANCE

A. Purpose and Output

13. The overall goal is to support Mongolia's continuing efforts to align accounting and auditing arrangements and practices with the needs of a market economy and with international best practices. To achieve this goal, the TA will assist MICPA to promote the adoption of IAS and ISA by enterprises through training and capacity-building programs that are geared to enhance the skills of accounting and auditing lecturers and professors as well as to develop a body of accountants and auditors who will be qualified for IAS and ISA.

B. Methodology and Key Activities

14. The key activities are in three areas.

1. Training in Accounting

- (i) Assist around 100 private enterprises in adopting IAS fully. At least one enterprise will be selected from each of the 21 provinces.

⁸ UNDP. *The Accounting Training Project*, for \$76,000, implemented in 1993 – 1994.

⁹ [ADB@1998. *Anticorruption Policies* \(On-line\). Available: http://www.adb.org/Anticorruption/default.asp](http://www.adb.org/Anticorruption/default.asp)

- (ii) Train 30 accounting teachers who will be teaching and advising on the introduction of IAS in small rural entities.
- (iii) Implement a training program for 20 Mongolian lecturers and professors who are nominated to take the CPA examination.
- (iv) Strengthen the capacity of the Accounting Policy and Methodology and Auditing Department of MOFE through a training course that will emphasize improving the professional skills and competence of 13 officers.

2. Training in Auditing

- (i) Develop and launch a training course on application of ISA for 200 Mongolian auditors from various audit firms¹⁰ (40 managers and 160 supervisors) who will specialize in the audit of commercial banks, insurance companies, educational institutions, private enterprises and projects implemented through foreign assistance. MICPA will charge an appropriate fee to the audit firms for participants attending the training courses.
- (ii) Assist MICPA to develop compulsory and uniform internal procedures that will help strengthen the capacity and capability of audit firms.
- (iii) Assist MICPA in setting twinning arrangements¹¹ with international audit firms for secondment programs to train 40 auditors on ISA. Expenses related to secondment programs will be covered by the audit firms.

3. Strengthening MICPA

15. MICPA will be strengthened in performing the following tasks.

- (i) Further improve the methodology of the CPA examination in Mongolia
- (ii) Develop a sustainable compulsory CPE program for CPAs
- (iii) Improve the ethical code for Mongolian CPA
- (iv) Improve the interaction of MICPA with other institutes in developed countries
- (v) Develop accounting and auditing manuals incorporating international standards
- (vi) Design a web page for MICPA and develop videotapes that include appropriate training components for auditing/accounting/CPE.¹²

¹⁰ Mongolia has 41 registered public accounting firms.

¹¹ It is common practice for international audit firms to enter into secondment arrangements for training of auditors.

¹² ADB's specialized training module prepared for Nepal will be translated into the local language and replicated by consultants on the web page.

C. Cost and Financing

16. The total cost of the Project is estimated at \$620,000 equivalent comprising \$342,000 in foreign exchange and \$278,000 equivalent in local currency (Appendix 2) costs. ADB will finance \$500,000 equivalent comprising \$342,000 in foreign exchange and \$158,000 equivalent in local currency costs. The Government will finance the remaining local currency costs of \$120,000. The TA will be financed on a grant basis from the ADB-funded TA Special Fund.

D. Implementation Arrangements

17. The TA will be implemented over 12 months beginning in November 2002. The TA provides a total of 19 person-months of consulting services: 11 international and 8 domestic. The consultants will be selected and engaged in accordance with ADB's *Guidelines on the Use of Consultants* and other arrangements for selecting and engaging domestic consultants. The consultants will be recruited as individuals. The accounting specialist will be the team leader and will take responsibility for the quality of the overall TA output. The consultants will produce an inception report and a draft final report due 2 weeks before the conclusion of the consultants' assignments. At the end of the assignment, the final report will be produced taking into account the comments of ADB, MICPA, and MOFE. The consultants' terms of reference are in Appendix 3.

18. MOFE will be the Executing Agency for the Project. To oversee the implementation of the TA on a day-to-day basis, a working group will be established with (i) officials from MOFE, (ii) members from MICPA, and (iii) professors of accounting and finance from academic institutions in Mongolia selected by MOFE. The working group will be principally responsible for overseeing the activities of the consultants. MOFE will provide office space and other logistical support, domestic transport, and other assistance necessary for preparing reports. The Government's contribution to the cost of the TA will be in kind. Equipment for the TA will be procured in accordance with ADB's *Guidelines for Procurement*. MICPA will also provide counterpart staff for each of the activities so that local staff can assist the consultants and learn. MICPA will be responsible for most of the document translation including the input documents, but excluding the consultants' reports, which will be financed by ADB. A TA office will be established to implement the TA. The project director will be the president of MICPA and the deputy project director will be the vice secretary general of MICPA.

IV. THE PRESIDENT'S DECISION

19. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$500,000 on a grant basis to the Government of Mongolia for Capacity Building for Accounting and Auditing Professionals, and hereby reports this action to the Board.

TECHNICAL ASSISTANCE FRAMEWORK

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Goal</p> <ul style="list-style-type: none"> Support aligning accounting arrangements and practices with the needs of a market economy and best international practices 	<ul style="list-style-type: none"> Expand the adoption of international accounting standards (IAS) and international standards of auditing (ISA) through training and capacity building programs Develop a body of accountants and auditors 	<ul style="list-style-type: none"> Feedback from Government, private sector, professional accounting and auditing practitioners Comprehensive ADB review after 6 months Progress reports submitted by consultants TA completion report 	<ul style="list-style-type: none"> Commitment of the Mongolian Institute of Certified Public Accountants (MICPA) and selected enterprises to implement recommendations Commitment of the selected accountants and auditors to adopt IAS and ISA
<p>Purpose</p> <ul style="list-style-type: none"> Upgrade the financial statements reporting of 100 private companies and financial institutions by helping them convert into international standards Improve the skills of accounting and auditing lecturers Develop a body of accountants and auditors who will be qualified for IAS and ISA Create a core group of trained people that will further help train others to enhance the multiplier effect of training 	<ul style="list-style-type: none"> Design training programs on IAS and ISA for qualified accountants and auditors Design a continuing professional education (CPE) program and strengthen its implementation Review the existing certified public accounting (CPA) examination and ethical code for CPAs and develop methodology for further improvement of the examination 	<ul style="list-style-type: none"> Review of consultants' report on technical assistance (TA) findings, and accomplishments by steering committee and task force Asian Development Bank (ADB) review missions Tripartite meetings Workshop to discuss draft final report 	<ul style="list-style-type: none"> Ministry of Finance and Economics (MOFE) and MICPA will provide full support to the TA Reports and training materials developed are available in local languages Training materials and programs are used
<p>Output</p> <ul style="list-style-type: none"> Increased acceptance of IAS Developed body of accountants and auditors who will be qualified for IAS and ISA Uniform internal procedures for audit firms enforced by MICPA 	<ul style="list-style-type: none"> Financial reporting in line with international standards Increase in the number of professional accountants and auditors that are qualified for IAS and ISA Strengthened 	<ul style="list-style-type: none"> Consultant report ADB review missions Tripartite meetings Workshop to review output 	<ul style="list-style-type: none"> Information is available in English Public and private sector practitioners support the activities Findings and recommendations will be sustained and shared with future accounting and auditing practitioners

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<ul style="list-style-type: none"> • A core group of trained people including accounting and auditing lecturers who will further help train others to enhance the multiplier effect of training • Improved capacity of the Accounting Policy and Methodology Department of MOFE • A compulsory CPE for CPAs • Accounting and auditing manuals that reflect international best practices • A web page for MICPA that includes appropriate training components for auditing/accounting/ CPE 	<p>guidelines on the supervision of audit firms by MICPA</p> <ul style="list-style-type: none"> • Revisions to CPA examination and CPA ethical code • Design of an effective training program for training of accountants in the rural areas • Resource and structural implications to implement plans as identified • Compulsory CPE program that keep accountants and auditors skills in line with the changes in the practice • A working web site that can be accessed by MICPA members 		<ul style="list-style-type: none"> • Training programs are effective • Changes to legislation are effected to implement recommendations
<p>Input</p> <ul style="list-style-type: none"> • TA of \$500,000 	<ul style="list-style-type: none"> • A team of three international consultants (11 person-months) comprising accounting and auditing specialists • Three domestic consultants (8 person-months) comprising accounting and auditing specialists • Research and workshops • Translation, miscellaneous administration, and support services • Training trainers program 	<ul style="list-style-type: none"> • Consultant report • ADB review missions • Tripartite meetings • Workshop and training evaluation reports 	<ul style="list-style-type: none"> • Timely engagement and mobilization of consultants • Data availability • Open discussions of relevant issues and options • Receptiveness to changes • Translation of materials completed

COST ESTIMATES AND FINANCING PLAN
(\$'000)

Item	Foreign Exchange	Local Currency	Total Cost
A. Asian Development Bank Financing ^a			
1. Consultants			
a. International – Remuneration	220	0	220
i. Per Diem and Air Fare	50	3	53
b. Domestic – Remuneration	0	50	50
2. Equipment ^b	15	0	15
3. Training and Workshops	0	80	80
4. Communication and Reports	10	0	10
5. Translation	0	15	15
6. Contract Negotiations ^c	7	0	7
7. Contingencies	40	10	50
Subtotal (A)	342	158	500
B. Government Financing			
1. Office Space and Logistic Support	0	105	105
2. Remuneration to Counterpart Staff	0	5	5
3. Others	0	10	10
Subtotal (B)	0	120	120
Total	342	278	620

^a Funded from the ADB Technical Assistance Special Fund.

^b Three computers, three printers, one photocopier, and a fax machine.

^c Includes cost of travel and per diem for Government observer invited for contract negotiations.

OUTLINE TERMS OF REFERENCE FOR CONSULTANTS

1. All consultants will be recruited according to the Asian Development Bank's (ADB's) *Guidelines on the Use of Consultants* and other arrangements for the selection and engagement of domestic consultants. ADB and the Government will review and evaluate the consultants' output. The expertise required, the job descriptions, and the person-months (given in parentheses) for each consultant are in paras. 2-10. A team of three international consultants for 11 person-months and three domestic consultants for 8 person-months will be recruited. Consultants will be accounting and auditing specialists. The international consultant designated as the team leader will assume overall responsibility for the team's output.

A. International Consultants

1. Accounting Specialist /Team Leader (5)

2. The lead accountant will be an experienced certified public accountant (CPA), or equivalent, with (i) experience in a major accounting firm; (ii) substantive knowledge of international accounting standards (IAS) and their introduction in a developing member country; and (iii) substantive experience in developing accountancy training materials and methods, ideally employing the latest technologies. As team leader, this consultant will be responsible for overall management of the technical assistance (TA) and the timely delivery of reports.

3. The consultant will undertake these tasks:

- (i) Assist 100 private enterprises in their efforts to convert their financial accounts and reporting formats to international accounting standards.
- (ii) Develop and implement for 30 accounting teachers a standard training program on the use of the IAS. The teachers will serve as trainers to disseminate the training developed to the accountants in the rural areas.
- (iii) Develop accounting manuals that reflect international standards and best practices and conduct training programs and workshops on their usage.
- (iv) Develop and implement training programs for capacity-building measures accounting for 13 officers of the Accounting Policy and Methodology and Auditing Department under the Ministry of Finance and Economy (MOFE). The emphasis will be on improving professional skills and competency.
- (v) Supervise the work of the domestic consultant for accounting.

2. Auditing Specialist (3)

4. The auditing specialist will be a member of the professional accounting body of an International Federation of Accountants (IFAC) member institute with (i) experience with major accounting and auditing firms; (ii) substantive knowledge of international standards on auditing (ISA), their translation and introduction in developing member countries; and (iii) substantive knowledge in developing and implementing training courses on the use and adoption of ISA.

5. The consultant will undertake these tasks:

- (i) Develop and implement training courses on the application of ISA for 200 Mongolian auditors from various audit firms (40 managers and 160 supervisors) who are specializing in the audit of commercial banks, insurance companies, educational institutions, and private enterprises, and implementation of foreign-assisted projects.
- (ii) Develop auditing manuals that reflect international standards and best practices and conduct training programs and workshops on their use.
- (iii) Review the existing internal procedures and structure of audit firms and analyze them by comparing with international best practices.
- (iv) Implement an effective secondment program for 40 auditors to locally based international auditing firms.
- (v) Develop and implement training programs for capacity-building measures in auditing for 13 officers of the Accounting Policy and Methodology and Auditing Department under MOFE. The emphasis will be on improving professional skills and competency.
- (vi) Supervise the work of the domestic consultant for auditing.

3. Examination and Quality Control Specialist (3)

6. The examination and training specialist will be an experienced CPA with (i) extensive theoretical and practical knowledge of professional accounting body arrangements and examination systems in developing countries; (ii) familiarity with the application of best practices; (iii) extensive experience in designing and implementing accounting and auditing training programs; and (iv) knowledge of quality control regimes for the accountancy profession. The consultant will be familiar with (i) the promulgation of the education committee of IFAC; (ii) the ongoing work of the Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) of the United Nations Conference on Trade and Development (UNCTAD); (iii) IFAC's Code of Ethics for Professionals; and (iv) other relevant IFAC pronouncements. The consultant will be experienced in developing accountancy training materials and methods, ideally employing the latest technology. In close cooperation with the other consultants, this consultant will have the following responsibilities:

- (i) Review and analyze the existing Mongolian CPA examination and certification system and develop improvements to the existing system that will be in line with international standards and best practices.
- (ii) Conduct training programs for 20 Mongolian lecturers and professors who are nominated to take the CPA examination.
- (iii) Assess and, if necessary, develop improvements to the existing framework that guides the ethical conduct of Mongolian CPAs.
- (iv) Implement appropriate improvements to further strengthen the supervision of CPAs conduct.

- (v) Assist in building the capacity of MICPA through proper exposure to other professional institutions in developed countries.
- (vi) Review the current system of providing continuing professional education (CPE) to practicing accountants and auditors, then develop and implement a sustainable compulsory CPE system for practicing accountants and auditors in the public and private sectors.
- (vii) Supervise the work of the domestic consultant in information technology in designing and implementing a web page containing various training programs in accounting and auditing. The training programs will be based on the accounting and auditing programs developed by ADB for Nepal.

B. Domestic Consultants

7. Three domestic consultants will be recruited under the program as follows: (i) accounting specialist (ii) auditing specialist and (iii) information technology specialist. ADB will select the three on the recommendation of the team leader and in consultation with MOFE.

1. Accounting Expert (3)

8. The accounting specialist will be a MICPA member, with theoretical and practical experience with Mongolian accountancy arrangements. In close cooperation with the international accounting specialist and the other consultants, the accounting expert will have the following responsibilities:

- (i) Assist in developing and implementing the training programs on the use of the IAS for 30 accounting teachers.
- (ii) Assist in developing accounting manuals that reflect international standards and best practices and conduct training programs on their use.
- (iii) Help develop and implement training programs for capacity-building measures in accounting for 13 officers of the Accounting Policy and Methodology and Auditing Department in the Ministry of Finance.

2. Auditing Expert (3)

9. The auditing specialist will be a MICPA member with theoretical and practical experience with Mongolian auditing arrangements. In close cooperation with the international auditing specialist and the other consultants, the auditing expert will have the following responsibilities:

- (i) Assist in completing of the whole translation of the IAS issued by the IFAC.
- (ii) Assist in developing and implementing training courses on the application of ISA for 200 Mongolian auditors from various audit firms.
- (iii) Assist in developing auditing manuals that reflect international standards and best practices and conduct training programs on their use.

- (iv) Assist in developing and implementing training programs for capacity-building measures in auditing for 13 officers of the Accounting Policy and Methodology and Auditing Department under MOFE.

3. Information Technology Expert (2)

10. The specialist will have these tasks:

- (i) Work with the examination and quality control specialist to implement a mechanism to promote the accounting and auditing training programs developed through the use of modern technology.
- (ii) Develop a web site that will help in disseminating the training programs and other information.