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# History of auditing in Russia. Periodization and challenges of development

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## Abstract

*This paper discusses the recent history of auditing in Russia from 1987 to the present time. This kind of research, such as any inquiry into history, calls for a well-grounded periodization. For the purposes of this study, factors were determined which influence the regulatory and methodological support of auditing; in accordance with the results of the analysis of their time intersections – the logical addition – qualitative leaps in the development of auditing in Russia were identified, which are represented as stages of its evolution. Through the application of this method, four stages in the recent history of auditing in Russia were identified: pre-history (the birth of the Russian auditing, the “wild” auditing); establishment of auditing in Russia; government regulation and licensing; self-regulation of audit activity.*

**Keywords:** Audit, history, historical stage, auditing standards, Russia.

**JEL Classification:** M42, M48.

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## Introduction

Auditing in its modern forms appeared in Russia in the second half of the 1980s, during the Perestroika period. It took almost 30 years, and today we have good reason to claim that “auditing has become one of Russia’s most successful business sectors” (Mennicken, 2010, p. 334). The recent history of Russian auditing also has its chroniclers and exegetes, both in Russia and abroad. The development of auditing in Russia and its first successes here were described in Enthoven et al. (1998). The chronology of auditing development in the light of its legislative regulation and of the evolution of its methodological framework were presented in sufficient detail in the monographs written by Sokolov and Terekhov (2004) and McGee and Preobragenskaya (2005). Samsonova-Taddei (2013) studied the evolution of a legislative framework for auditing in Russia as a local site of globalization, and, in particular, the responses of local audit firms to the implementation of International Standards on Auditing (ISAs) in Russia. Sucher and Bychkova (2001) have identified the auditor independence rule requirements that have been implemented into the laws and codes of practice in Russia. Menniken (2008), taking a large post-Soviet Russian audit firm as an example, described the circulation of international auditing standards in Russia as one of “connecting worlds” and translation. In Menniken (2010) the roles that images and ideas of market creation played in the re-articulation of relations between government, audit expertise and professional organisation in post-Soviet Russia are discussed. The case of one of the biggest Russian companies Gazprom and its auditor, PricewaterhouseCoopers, is regarded as an example of globalization and multinational auditing by Alon and Dwyer (2012).

Thus, some aspects of the recent history of auditing in Russia have attracted researchers’ attention or have been investigated in multiple publications. Meanwhile, the duration of these transformations provided a reasonable basis for interpreting the changes as a complete process. The author of this paper considers that this kind of research requires a well-grounded periodization.

## 1. Research hypothesis

This study is aimed at creating a periodization of the development of audit activity in Russia with the

help of the operation of logical addition on chronological climaxes of regulatory and methodological development of auditing. Qualitative leaps in the development of auditing are described by a set of factors influencing the legislative and technological support of auditing.

Criteria of periodization or factors relevant for the development of auditing in Russia, in our opinion, are as follows:

1. A major change of legislation in the field of audit;
2. Improvements in the standardization practice of audit activity;
3. A change in auditing techniques;
4. Evolution of the independence principle;
5. Introduction of ethical standards and codes of professional conduct for auditors;
6. Integration of the Russian auditing into the international system;
7. Changes in the forms of audit reports;
8. Situation on the Russian audit market;
9. Development of types of audit business activities;
10. Evolution of the academic coverage of audit theory and practice.

Each of the factors has its own chronology of development. Their logical addition should create qualitative leaps in the development of audit activity, which can be represented as stages in the development of auditing. We have essentially a matrix in which the horizontal axis shows the factors of influences and the vertical axis the time-series representing the operation of a given factor.

It is important to note that these factors play different roles in the development of auditing. For the purposes of this study, they can be divided into “active” and “passive”. The active factors cause changes and development of other factors, while the passive factors result from the influence of other factors. For instance, the adoption of a new law on audit (an active factor) can lead to major changes in the audit market and in auditing techniques (passive factors). Let us consider the chronology of the development of the criteria listed above.

## 2. Chronology of the factors influencing the development of auditing in Russia

### 2.1. A major change of legislation in the field of audit

The change of auditing legislation is an active factor for the development of auditing in Russia. The chronology for the emergence of this factor is connected with the adoption, on September 8, 1987, of the Resolution of the Union of Soviet Socialist Republics (USSR) Council of Ministers on "Creating a Soviet Audit Organization". Pursuant to the provisions of this resolution, a corporation for providing audit services, *Inaudit*, was established under the auspices of the Chief Directorate of Monetary Control at the USSR Ministry of Finance. Regulatory control over auditing in Russia was at the initial stage of its development. In 1991-1993, a draft law on "Audit Activity" was prepared. This was, in fact, a period of "wild" voluntary audit in the Russian Federation, which was based on a variety of different principles, starting from the rules of statutory audit to international auditing standards (used by the then Big Six, now the Big Four companies).

Presidential Decree No. 2296 of December 12, 1993 introduced the first rules regarding the audit activity in the form of "Provisional Rules of Audit Activity", which define auditing as an independent business activity. These rules, together with subsequent Resolutions adopted by the Government of the Russian Federation, established a system of auditor certification and licensing of audit activity. Four types of auditor certificates and licences were introduced:

- General audit;
- Bank audit;
- Insurance audit; and
- Audit of commodity and stock exchanges, off-budgetary funds and investment institutions.

Provisional rules of audit activity were the first general standards for auditing in Russia; they gave a definition of auditing and its types, asserted the principles of auditing as well as the rights and responsibilities of the auditor and the client, and also types of audit reports. A rapid growth in the number of auditors and audit firms followed, owing to the development of the mandatory

auditing market. The first generation of auditing standards appeared, approved by the Commission on Auditing Activity under the President of the Russian Federation.

The first Federal Law on "Auditing" No. 119-FZ of July 13, 2001 consolidated the statutory framework for auditor certification and licensing of audit activity. New types of Federal Standards of Auditing Activity (FPSAD) were introduced, which greatly facilitated the rapid growth of the auditing market.

Changes in the mechanism of audit regulation were heralded by the adoption of the new law on "Auditing" No. 307-FZ of December 30, 2008. The institution of self-regulation of audit activity and a single auditor's qualification certificate were introduced in Russia. Six self-regulatory organizations (SROs) of auditors were established and began to work, of which five continue to operate today:

- Audit Chamber of Russia;
- Institute of Professional Auditors;
- Moscow Audit Chamber;
- Russian Collegium of Auditors; and
- Auditor Association Sodruzhestvo.

Changes in quantitative requirements for mandatory auditing, the need to retake an exam in order to obtain new auditor qualification certificates, and tightening of quality control over audit activity led to stagnation on the audit market and a sharp reduction in the number of auditors and audit firms.

### 2.2. Improvements in the standardization practice of audit activity

Improvements in the standardization of audit practice are also an active factor for the development of auditing in Russia. Prior to 1996, auditing in the Russian Federation had been carried out based on company internal auditing standards. Russian auditing practices led to the formation and, thereafter, to the application of three generations of auditing standards nationwide. Currently, the transition to ISAs has been pronounced.

*The first generation* of Russian auditing standards, which all in all numbered 39 standards, was developed in the period 1996-2001 and approved by the Russian Federation Presidential Commission on Auditing Activities. Content-wise, they comply with system-oriented auditing.

The second generation of auditing standards, also known as Federal Rules (Standards) of Auditing Activities (FPSAD), was developed between 2002 and 2008. Altogether, the Government adopted 34 rules which were created on the basis of IASs analysis and, in essence, have acquired certain elements of risk-oriented auditing technologies.

Following that, between 2010 and 2011, the Russian Federation Ministry of Finance developed and adopted 11 Federal standards of auditing of the third generation. Content-wise, these standards closely approach those of ICA. The latest standards are supposed to be the final stage in preparation to the ICA transition, planned for the year 2014.

### 2.3. Changes in auditing techniques

The change of auditing techniques is a passive factor. Russian audit originated on the basis of revision technologies, which to a greater extent are similar to the compliance audit, i.e. with the testing of the company accounting standards (Guzov, 2013), intuitive determination or ignoring the level of materiality, risks and sampling.

The complexity in defining the chronological order, in which a certain dominant audit technology was applied, can be explained by stratification of audit firms, their division into major, medium-size and small ones, also by the failure to obtain the objective data on the auditors' application of internal audit standard rules (Guzov and Savenkova, 2013; Guzov, 2014).

In fact, from the very beginning major international audit companies (primarily the 'Big Four') started application of risk-oriented technologies in Russia in the beginning of the 1990s (Guzov and Strel'nikonikova, 2015). More than that, these companies also train their employees using Association for Chartered Certified Accountants' (ACCA) and Certified Public Accountants' (CPA) programs the successful completion of which was emphasized as a prerequisite for partnership in the said companies.

Realization of TASIC project *Audit in Russia 1* in 2001 facilitated the mastery of risk-oriented technologies by major Russian audit companies. Work procedures and technology package of operational documentation applied in audit was laid open to public. The fact that major Russian audit companies joined international audit networks and won international audit tenders may serve

indirect proof of their successful mastery of the technologies (Guzov and Strel'nikonikova, 2015).

In the period between 1996 and 2008 Russian small and medium-size audit companies were mastering system-oriented audit techniques based on auditing standards. It seems that transition of small and medium-size audit companies to risk-oriented technologies is now at its beginning, since outside control reveals these companies' typical mistakes, i.e. a low level of audit planning, the failure to carry a review engagement before the auditor's opinion is formed, also the failure to provide a sampling description and risk assessment (Current problems, 2013).

### 2.4. Evolution of the independence principle

The evolution of the independence principle is a passive factor. In the "wild" audit period it was possible that the independence principle was neither observed, nor controlled. Specified inclusion of this principle dates back to 1993; first declaration forms were filled in 2002, and the feasible check into its observance started between 2005-2008 after Provisional guidelines and the program for professional associations accredited by the Russian Federation Ministry of Finance to carry on checks into the audit services quality and after FPSAD 'Quality Services Control in Audit Companies' were adopted.

In 2012 they worked out "Rules of auditors" and audit companies' independence. They provided a conceptual approach towards the observance of independence and its application, and also an auditor's formal opinion report including instruction as to the restriction in its use and disclosure. The Rules provide a detailed understanding of an auditor's independence.

### 2.5. Introduction of ethical standards and codes of professional conduct for auditors

The introduction of ethical standards and codes of professional conduct is an active factor in the development of Russian auditing. In the beginning of the 1990s Auditors' Chambers in Russia started at their own and sole discretion to draw up ethical rules of conduct for auditors. The first Professional ethics code for auditors in Russia was elaborated and adopted in 2003 (as amended in 2007).

The new law on “Auditing” passed in 2008 made it binding for auditors in Russia to observe Professional ethics code. Currently in operation is Professional ethics code for auditors adopted in 2012. It includes basic ethics principles, a conceptual approach to their observance and application in concrete situations. Without prejudice to the parallelism of the Russian Code and International Federation of Accountants (IFAC) Code of Ethics, Russian auditors insist on direct descent of ethics principles from Immanuel Kant’s categorical imperative, the ethics and metaphysics of which are rather popular among representatives of professional and academic communities.

## 2.6. Integration of Russian audit into the global system

Integration is an active factor which contributed to the development of Russian auditing. Two stages can be distinguished in the process of Russian audit integration into the global system.

The first one dates back to the years 2001 to 2006, and corresponds to the acquisition of technical aid from international organizations (TASIS project *Audit in Russia 1 and 2* – translation of ISAs in order to facilitate federal auditing rules).

The second stage was connected with the declared adoption in 2014 of international audit rules and the expected (in connection with that) engagement of Russian experts into their elaboration.

## 2.7. Changes in the forms of audit reports

The changes in the forms of audit reports is a passive factor. The first Russian auditing standard dates back to 1996 and is known as the “Audit Opinion Report”. It was prepared to a major extent owing to the lobby of the Big Four companies and compiled on the basis of ISAs. It introduced the following types of formal opinion reports,

i.e. unqualified opinion, qualified opinion, adverse opinion and also the disclaimer of opinion. The 2010 standard rules implemented non-modified and modified audit opinion reports. Also defined was the “decision-matrix” system connected with the typology of auditor opinion modification including considerable non-comprehensive and comprehensive influence.

## 2.8. Situation on the Russian audit market

The situation on the audit market is a passive factor. Judging from some estimates, in the time of the “wild” audit there were around 800-900 audit firms, with up to 5,000 practicing auditors.

The first statistical survey of the Russian audit market was launched in 2006. Results of the expert analysis showed that somewhat 4,500-5,000 audit firms actually carried on business on the audit market in 2005. For the purposes of the market analysis of audit services and relying on the credibility and accuracy of the available data, the number of audit firms in Russia in the year 2005 (i.e. within the time interval fixed through expertise) could be set at 4,700.

The development of the audit market of the period 2004-2008 is characterized by a quick growth of audit income, of the number of auditors and clients of audit firms. Yet, the level of modified audit opinion reports remained at approximately 40-50%.

Major quantitative indices of the audit market development in Russia in the years 2009-2013 are shown in **Table 1**. The development of the audit market in the given period is characterized by stagnation of the audit firms’ income. Implementation of self-regulation in audit profession and a new unified qualification certificate is followed by a dramatic decrease in the number of auditors, yet, with the number of audit firms remaining stable. Likewise, noticeable is the drastic decrease in the level of modified audit reports issuance.

**Table 1. Russian audit market in the years 2009-2013**

Year	Audit firms’ income (bln. rubles)	Number of audit firms (thousands)	Number of auditors (thousands)	Number of clients (thousands)	Level of modified audit reports issuance (%)
2009	49.6	6.9	38.8	92.7	44.2
2010	49.1	6.3	26.3	60.6	41.4
2011	50.0	6.2	26.8 (1.1)	75.6	33.8
2012	51.0	5.7	24.1 (3.2)	70.0	29.0
2013	52.2	5.5	23.0 (3.2)	68.4	25.9

Source: Authors’ processing, based on the main indicators of the audit services market in the Russian Federation.

The trends for the stagnation of the audit firms' income and decrease in the number of auditors are likely to carry on in the nearest future.

## 2.9. Development of types of audit business activities

The diversification of audit activities is a passive factor. Alongside with the development of audit practices, there appear new technologies for consulting business and outsourcing bookkeeping and accounting services. As compared to the year 2005 when the share of non-audit activities in audit firms combined income equaled 35%, in the year 2008 this figure was 40-55%, and in 2013 it was already 46-63%. In other words, currently regional audit companies generate their principle income from consulting and accounting services.

In an indirect way this trend evidences intensification of the audit market monopolization.

## 2.10. Evolution of the academic coverage of audit theory and practice

The evolution of audit in the academic environment is an active factor. In the 1990s much work was done under the editorship of Professor Y.V. Sokolov to have publications on audit translated from foreign languages. Thus, books by such authors as Adams (2005), Arens and Loebbecke (2001) saw light, as well as the translated standard textbook "Montgomery's Auditing" (Defliese et al., 1997). Publications released within the framework of TASIC project *Audit in Russia 1* have made a vast contribution into the development of risk-oriented audit techniques. To summarize the project results a monograph by Remizov and Tabalina (2003), "Auditing: Modern methodology: Audit of Financial Statements in Compliance with ISAs and Federal Standards on Audit Activities (FPSAD)" (2003), was published. For the first time in history this book described Russian interpretation of risk-oriented audit programs.

There followed a series of profound research materials published in that period. Among them, there were: the research work by Skobarya (1998)

dedicated to audit documentation flow; Bychkova and Gazaryan (1998) on audit planning; Bychkova and Rasmathanova (2003) on risk appraisal; Bychkova (1998) on audit evidence; Eliseeva and Terekhov (1998) on sampling in audit.

Unfortunately, as a general rule, the textbooks on audit published in great numbers in the last twenty years describe technologies of compliance audit and of the checks into regulatory bookkeeping and accounting. This evidently leads to the fact that employees working for small and medium-sized audit firms fail to have a good handle in risk-oriented audit technologies and are very sensitive to whatever novelties are being introduced into audit standard rules.

Russian audit journals are generally focused on discussing issues in connection with the adaptation of audit standard rules and realization of audit programs. Independent academic studies in the sphere of audit are practically non-existent. No wonder that representatives from Russia rather seldom make reports at the European Congress of accountants. Such state of things, on the whole, indicates a serious information lag which a good number of Russian audit firms experience concerning modern risk-oriented technologies of auditing. In 2013-2014 St. Petersburg State University was one educational organization which has a joint diploma with ACCA. And this is now becoming a general trend in Russian leading higher schools.

## Conclusions

Logic addition of the considered chronological order of factors presents the history of audit development in Russia divided into the following time periods (Table 2):

- Period 1. 1987-1993: *Prehistory* (origination of Russian audit, i.e. "wild" audit);
- Period 2. 1993-2001: *Formation of audit in Russia*;
- Period 3. 2001-2008: *Government regulation and licensing*;
- Period 4. 2009 until currently: *Self-regulation of audit*.

**Table 2. Log frame matrix for monitoring factors affecting the development of audit in Russia**  
(Yes – available influence; No – absence of influence; A – active factor; P – passive factor)

Impact factors	1987-1993	1993-2001	2001-2008	2009-present
1 – A	Yes	Yes	Yes	Yes
2 – A	No	Yes	Yes	Yes
3 – P	No	Yes	Yes	Yes
4 – P	No	Yes	No	Yes
5 – A	No	No	Yes	Yes
6 – A	No	No	Yes	Yes
7 – P	No	Yes	Yes	Yes
8 – P	No	Yes	Yes	Yes
9 – P	No	Yes	Yes	Yes
10 – A	No	Yes	Yes	Yes

Source: Authors' processing.

The content of the present-day stage of audit development in Russia is highlighted by the developing system of self-regulation, the transition to international standard rules in auditing and to risk-oriented technologies, in the circumstances of the

audit market stagnation, the dramatic decrease in the number of auditors, the information lag and publication scarcity in terms of audit innovations coverage and of intensification of the system of audit quality control.

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