

# Russian industry charges ahead

The Russian accounting industry is young and growing at a breakneck speed. Industry leaders speaking to **Carolyn Canham** place fee income growth of the profession as a whole at close to 40 percent, and there is little sign of it slowing

In the inaugural *International Accounting Bulletin* survey of the Russian accounting profession, the overall fee income was RUB26.6 billion (\$1 billion). Kreston International had the highest revenue growth – 122 percent – for the year ended October 2006. Its fee income of RUB646.5 million was the eighth highest recorded in the survey.

SC International (SCI) also more than doubled its fee income, growing 121 percent to RUB310 million. The association of independent firms picked up two new Moscow members during the past year, bringing its total number of offices to five.

## IFRS audit in demand

Elena Yuzhakova, the deputy director of SCI Moscow member firm International Consulting and Legal Centre (ICLC), says one of the service lines that performed well was audit. “Not only audit under the Russian standards, but audit under the IFRS as well, because the IFRS audit is now in great demand in Russia,” Yuzhakova notes.

In 2004, the Russian Ministry of Finance set 2010 as the date by which all companies are expected to comply with IFRS. Although most firms find Russian standards are still more in demand, many experienced growth in IFRS work.

“Clients that require audit under IFRS include Russian companies that have plans to expand to international markets, for example the London stock exchange, companies with foreign investments and branches of [international companies expanding into Russia],” Yuzhakova says.

“For small business and medium business in the near future, IFRS audit is not as relevant as for large clients,” she continues, adding that the process of conversion between Russian standards and IFRS is “quite active” and due to the growing demand for IFRS audit, companies “do their best” to be involved with the conversion process.

BKR Intercom-Audit audit partner Yulia Emelianova concurs. “Now it is very popular in Russia to prepare the financial statements according to international standards and this type of service has good prospects,” she

says. However, again, Russian standards are in more demand. Emelianova estimates the firm has 170 clients for Russian audit and about 50 for international.

Moore Stephens Russia’s overall growth for the year ended December 2006 was 22 percent. It reported fee income of RUB297.1 million. The international network’s Russian offering comprises a national member firm with five offices, plus a selection of associate firms. Moore Stephens Russia managing director Gavin Stoddart estimates the growth for the full member firm offices stood at about 30 percent. He attributes this to IFRS.

“Our work is mainly to international standards,” he explains. “The firms which do work in accordance with Russian standards, I think their growth is slower, because the market is just not as hot for the statutory audit as it is for the audit to international standards and for activities like [initial public offerings (IPOs)] – there have been an awful lot of IPOs going on.

“What has been really significant has been that over the last few years you’ve got a lot of the medium-sized Russian firms listing abroad. The Alternative Investment Market [AIM] has been very popular.”

He says the movement among medium-sized firms is of particular interest to Moore Stephens. “Where before anybody who was raising finance internationally was probably a Big Four client, I think now they [include] the sort of companies that are very naturally Moore Stephens clients,” he explains.

## Rapid growth

Estimates from the firms that spoke to IAB put the growth of the Russian accounting industry at close to 40 percent during 2006. Yuzhakova suggests one of the reasons for the rapid rate of growth is that the audit profession is “very young”. She says the 20th anniversary of the profession in Russia was celebrated in September this year.

Another reason for the growth is the Russian economy, which Stoddart describes as “booming”. “I think if it wasn’t for China, there would be a lot more talk about the Russian economy. It has been performing very, very well consistently for the last four or five

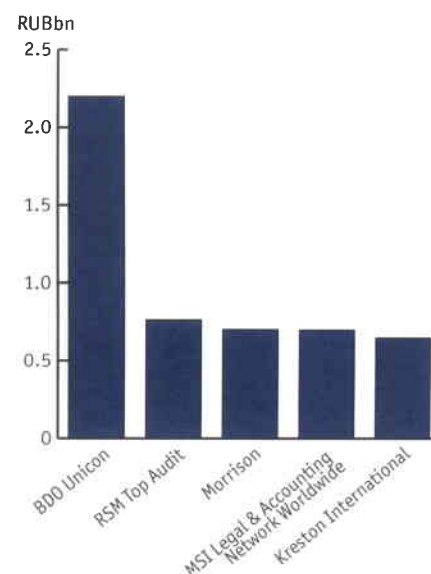
years,” Stoddart claims, while adding that he doesn’t see any reason why high growth levels should not continue.

“There were some reforms which obviously helped kick-start things,” Stoddart explains. “When [Russian President Vladimir] Putin first came in [to office] he made some changes to tax legislation, which I think were very positive, but then the big drive has just been the oil price. And Russia is such a big producer of oil and gas; 25 percent of the world’s reserves are here. So while the price is high it is very good for the economy. And then on top of that, what’s good with Russia is you’ve got a highly educated population and so you get the knock-on effect, it doesn’t just stop in the raw materials sector, it can go right the way through, you’ve got people who can set up businesses right across the sphere.”

BDO Unicon international desk director Philip Gillen also suggests that continued growth in the Russian GDP would be a reasonable expectation. “We are effectively two months away from parliamentary elections and have just had a change of government, but the Russian markets haven’t even

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### Top five mid-tier fee incomes: 2007



Source: IAB

missed a beat," he says. "There is of course significant interest in the election process and speculation about who will run for president, but the overall expectation is that the positive business trend of the past few years will continue."

Gillen says the ongoing growth will be a challenge to manage. "But we have placed a particular emphasis on strengthening and enhancing our [human resources] capabilities to meet these challenges. Candidly, we look forward to the possibilities offered by such growth and view this as a wonderful opportunity to develop the next, or perhaps even the first, real generation of business leaders in Russia," he says.

### The worldwide challenge

Despite a highly educated work force, the Russian accounting industry shares the worldwide problem of a skills shortage. Both Stoddart and Barnes say the limiting factor for growth is identifying and retaining high calibre people.

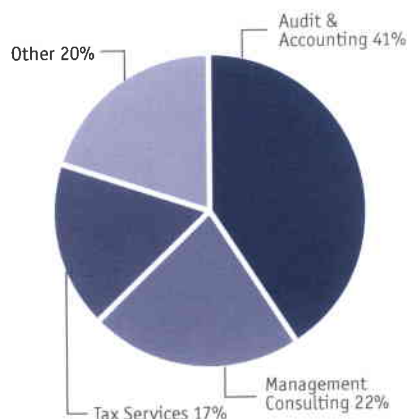
Stoddart says: "If we had more staff, we would grow faster. I hope that we can find the staff [we need] and we're putting a lot of effort into growing our own, because you just can't get enough in the market." Stoddart says this is especially the case for Moore Stephens because the majority of the firm's work is international: "What we're really after are people who have got internationally recognised qualifications. That's where the growth in the work is and we need people who can do that work and can do it to the right standards, and there is a real deficit."

Vladislav Yermizin is president assistant for international affairs at MSI FDP-Aval, a group of companies that is a member of MSI Legal and Accounting Network Worldwide (MSI). He says finding and retaining enough "highly professional" staff is the firm's biggest problem. "The need for highly professional staff is increasing because the customers are becoming more demanding and they need specialists of higher rate," he says. "The number one thing for us is not to lose our current staff. Our retention is very important for us and so for those purposes we do a number of actions, for example monitoring the professional development."

One method employed by several of the firms to retain staff is to provide constant training and development.

Yuzhakova agrees that one of the main challenges in audit practice in Russia is finding the qualified skilled personnel. She also points to another challenge facing the industry – audit quality. The SCI representative explains that it is "rather easy" to establish an audit company in Russia, therefore there is a proliferation of small and very small audit companies. Yuzha-

### RUSSIA Mid-tier fee split: 2007



Source: IAB

kova says this drags down audit prices and can "very often" prejudice the quality.

"Also," she says, "it's necessary to mention [the] unjustified complexity of Russian accounting standards and steps on their simplification should be taken." Yuzhakova suggests legislation is required to resolve both these problems.

Baker Tilly International chief executive and president Geoff Barnes says steps are being taken to address audit quality. "I am told in a year or two's time, 2009, all those holding a licence to audit will have to reapply to their institute to get permission, because they want to try and strengthen and streamline those that actually undertake audits," Barnes relates. "So for those good firms, those strong firms, like us, there are great opportunities during this period."

### Little transparency

The top tier of the Russian audit profession lacks the transparency enjoyed in other parts of the world. Although the mid-tier firms were happy to disclose fee income, growth rates and staff numbers, the Big Four were less forthcoming. The Russian member firm of PricewaterhouseCoopers (PwC) was the only Big Four firm to disclose to IAB its fee income and an estimation of its staff numbers. MSI's Yermizin says he assumes that Russian legislation allows the Big Four to choose not to release their figures. He says most Big Four firms do not submit their information to Russian rating agencies.

PwC has been in the news during the year due to a legal battle with the country's tax authorities over claims that it did not conduct *bona fide* audits of failed Russian oil company Yukos. The Russian Tax Inspectorate 5 is seeking \$150,000 in audit fees from PwC for audit work it carried out on Yukos's accounts in 2002, 2003 and 2004.

According to PwC, the tax collector's claim is that the firm should have been aware of and alerted authorities about Yukos's tax schemes, which have been determined to be illegal by the Russian court.

In June this year, PwC withdrew ten years of audit reports for Yukos. The firm said at the time that the reports for 1995 to 2004 should "no longer be relied upon" due to information that has recently come to its attention. PwC now believes information and representations that were provided by Yukos's former management may not have been accurate.

Moore Stephens's Stoddart suggests the Yukos affair has not had much of an impact on the accounting industry in Russia. "Perhaps not as much as you would have expected it to [be], to be honest. I think even possibly there's more wariness at a general level abroad than there is in Russia, I don't think it has been particularly widely publicised," Stoddart suggests.

### Big Five

The Russian accounting industry has a clearly defined Big Five. BDO Unicon is hot on the heels of the Big Four in terms of fee income and staff levels, and is almost three times the size of RSM Top Audit, the sixth-largest firm. BDO Unicon is not only large, it is growing rapidly. The firm reported fee income growth of 41 percent to RUB2.198 billion for the year ended December 2006.

Gillen from BDO Unicon said the firm's IFRS-adjusted accounts show an even higher rate of growth for the whole of the BDO Unicon group. "The heart of the matter for us has been, and is, to persist in doing the right things day-in day-out and month-in month-out. This is about preparation and opportunity," Gillen says.

He tells IAB Unicon worked for many years in Russia without an international affiliation. "So all we had to rely on were our own resources, and there was a fiercely competitive will to succeed," he continues. "Clients and the market make cold judgements and for now we have had some success, so this is nice, but we cannot afford to be complacent in any way."

In terms of whether the dramatic growth is likely to be repeated, Gillen suggests: "We expect to keep doing the right things – financial numbers are a nice indicator, but are not the only measure. For now let's just say we're looking forward – positively."

Gillen says the firm is "pleased with all areas of the practice this year". He adds the outsourcing division has done well, growing from a small initial base, and the audit and consulting businesses have performed strongly during the year. "Our regional network has

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## Leading accounting firms and associations 2007: fee data

FIRM/INTERNATIONAL AFFILIATE	Most recent year's fee income (RUBm)	Growth rate (%)	Fee split (%)							Year-end
			Audit & accounting	Tax services	Management consulting	Corporate finance	Corporate recovery/insolvency	Litigation support	Other	
<b>FIRM/INTERNATIONAL AFFILIATE</b>										
PricewaterhouseCoopers Russia (7)	5,559.0	-	-	-	-	-	-	-	-	Jul-06
Ernst & Young Russia (e)	4,700.0	-	-	-	-	-	-	-	-	-
Deloitte & Touche (e)	3,948.0	-	-	-	-	-	-	-	-	-
KPMG (e)	3,384.0	-	-	-	-	-	-	-	-	-
BDO Unicon (7)	2,198.0	41	45	7	36	6	-	-	6 (4)	Dec-06
RSM Top Audit	762.0	18	31	9	48	-	-	-	12	Dec-06
Gorislavtsev/Euraudit International	238.0	4	47	12	10	7	4	6	14	Jun-07
JSC Grant Thornton	188.0	96	49	11	-	37	-	-	3 (3)	Dec-06
Baker Tilly Russaudit	182.9	40	63	7	7	8	-	-	15	Jun-07
BKR-Intercom-Audit	150.0	24	57	19	-	13	6	-	5	Jul-07
Rödl & Partner (7)	107.1	68	47	11	-	-	-	42	-	Dec-06
<b>ASSOCIATION OF INDEPENDENT FIRMS</b>										
Morison International	700.0	-	29	-	29	24	-	18	-	Dec-06
MSI Legal & Accounting Network Worldwide (1)	697.3	12	7	89	-	2	-	-	2 (2)	Dec-06
Kreston International (5) (7)	646.5	122	45	27	19	4	1	-	4	Oct-06
PKF Russia (7)	557.9	9	67	20	11	-	-	-	2	Jun-06
RBS/Horwarth International	478.9	38	27	9	43	3	-	3	15	Dec-06
Nexia CIS (7)	350.6	34	23	-	37	29	-	10	1	Dec-06
SC International (7)	310.0	121	52	13	26	-	-	-	9	May-07
Polaris International	308.7	-9	-	-	-	-	-	-	-	Jul-07
Moore Stephens Russia (7)	297.1	22	70	2	20	2	-	-	6	Dec-06
HLB Russia (7)	292.0	11	57	11	-	6	-	-	26	Dec-06
Alliott Group (7)	237.2	-	20	2	60	-	-	18	-	Dec-05
UHY International (6)	153.0	47	27	7	18	15	-	10	23	Dec-06
JHI	90.3	-	11	10	-	5	-	-	74 (3)	Aug-06
MGI	61.5	10	-	-	-	-	-	-	-	Jun-06
<b>Total revenue/average growth</b>	<b>26,598.0</b>	<b>49</b>								

Notes: (e) = IAB estimate. (1) MSI Legal & Accounting Network Worldwide is a multi-disciplinary network; however, this year's fee income does not include law firms; (2) Other includes appraisal services and IT consulting; (3) Other includes legal services; (4) Other includes accountancy; (5) Fee income includes RUB69.3 million from correspondent and non-exclusive member firms; (6) Figures are combined from two UHY member firms - Atomic Audit and Eccon; (7) Fee split figures are from fiscal year 2006.

Source: IAB

also been a significant contributor to the growth as this has become more integrated into the network," Gillen says.

JSC Grant Thornton, UHY International and Baker Tilly Russaudit also achieved growth above the estimated industry average. JSC Grant Thornton grew 96 percent to RUB188 million, UHY grew 47 percent to RUB153 million and Baker Tilly Russaudit grew 40 percent to RUB182.9 million.

Barnes says Baker Tilly International is "very pleased" with what the Russian firm has done. "The Russian economy seems to be on the move, the requirement of companies for professional services is clearly increased and the growth has been across the board," Barnes says. "Very strong improvement on the audit

fee income and certain M&A work as well, so it has been an exciting time for them."

Barnes explains that the M&A work has involved a mixture of Russian and international companies. "A certain [number] of the Russian clients are getting involved with mergers and acquisitions. The major investors in Russia at the moment are the Dutch and the Germans... and that's been a big development potential." Barnes says Russaudit has also assisted clients listing on the AIM in London, where they've worked in conjunction with Baker Tilly in the UK.

Horwarth International member firm JSC - Audit-Consulting Group Business Systems Development (RBS) recorded fee income growth of 38 percent to RUB478.9 million

for the year ended December 2006. The firm's deputy chief executive, Sergey Shwartsman, says the result was in line with the firm's corporate development strategy and 2006 business plan. "We have exerted every effort to maintain the growth dynamics and to successfully reach the goals aimed at increasing our market share," he says, adding the firm has great potential for more development.

Shwartsman says RBS has been traditionally strong in promoting management consulting services. "At present, the Russian administrative reform is in full swing," he explains. "Many markets undergo structural changes. The developing market economy requires a high level of professional training and qualification and quality of consulting