JSC GAZPROM

ENXHI NALLBANI

SABINA KALDYBEKOVA

Overview of Russia

In 1991 Soviet Union collapsed and it started a massive reorganization of Russia’s political, social and economic infrastructure

During 1992-1999 the Russian government implemented a “privatization programme” (75% of Russian companies were handed over to private sector)

This was quickly converting Russia from a controlled economy to a free market economy

The flaws

- Were allowed thousands of the individuals (Red Directors) who had been part of the Communist Party and overseen the formerly state-owned businesses to acquire top management positions in the newly organized companies
- The old mentality “cling to the view that the enterprise is an engine to generate wealth for themselves”
- The Russian accounting standards were poorly suited to market economics
- The legal system was undeveloped, leaving room for manipulation and theft

Introduction

- Gazprom is a huge Russian company operating in the gas industry

- It was the prime example of the “rogue capitalism in Russia

- It was created by officials of Soviet Union to control the country’s natural gas industry

- 15% of Gazprom stocks was given to employees
- 28% of stocks—owned by customers
- 40% ownership interest was retained by federal government
- The rest of stocks was sold to foreign investors

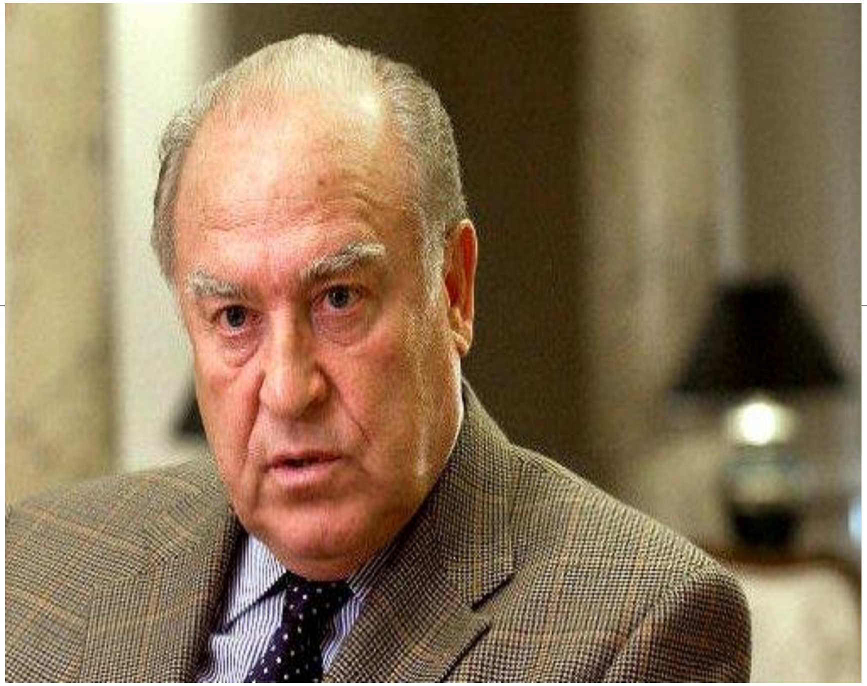
During 1990’s GAZPROM was the largest and the most important Russian company

Gazprom accounted for

- nearly 10% of Russia’s gross domestic product
- 20% of its exports and tax revenues
- Had 400’000 employees
- Provided directly or indirectly a livelihood for more than 6mln Russians
- Supplied more than one-half of natural gas used in Europe
- Controlled one-third of the world ‘s natural gas reserves

In 1995- Gazprom’s initial stockholders’ meeting was held

PwC (a British accounting and audit firm) was selected by The Board of Directors as the company’s audit firm



Rem Vyakhirev was Gazprom's top executive and the closest partner of Victor Chernomyrdin

Victor Chernomyrdin was the chief executive of Gazprom company in the first era and then he was elected as the Prime Minister of Russia

After being resigned by V.V.Putin, in 2001 Forbes reported that the two former Russian peasants were among the 500 richest individuals in the world. Forbes pegged Vyakhirev's personal wealth at $1.5 billion, while Chernomyrdin's more modest fortune was estimated at $1.1 billion.

Wildest Dream or Worst Nightmare?

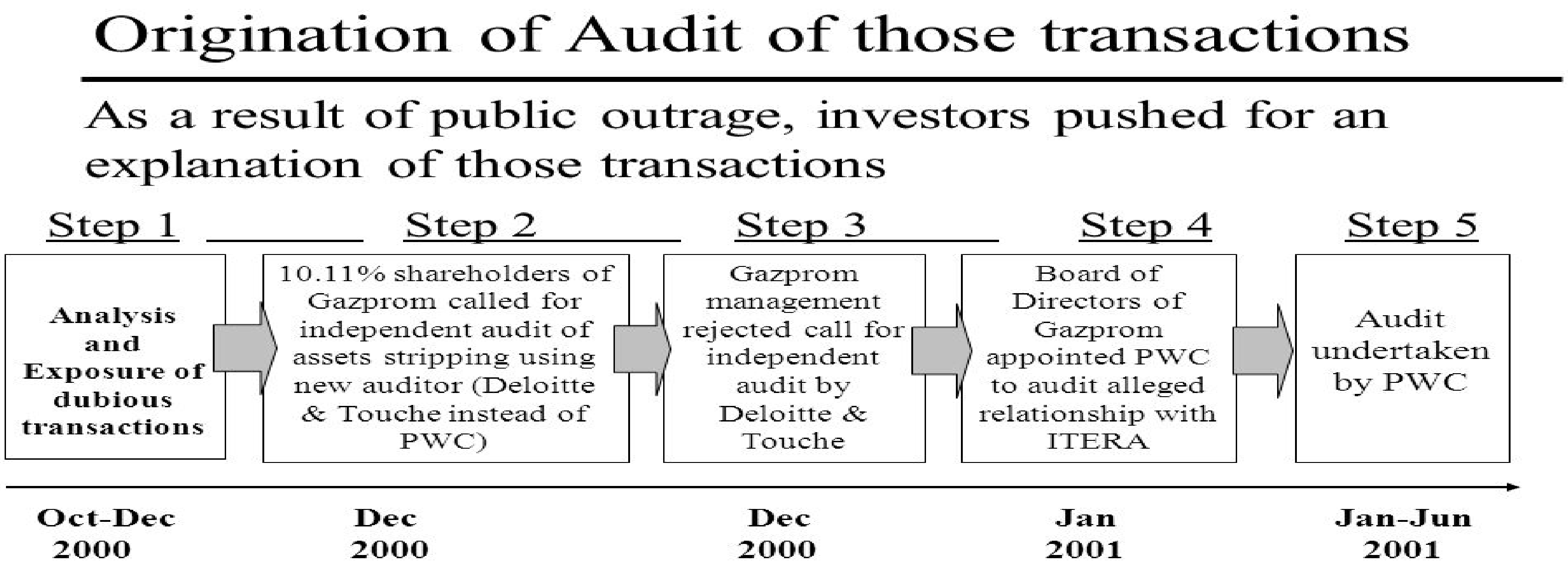
1. Gazprom sold a large volume of natural gas to Itera for **$2 per cubic meter**, which Itera then resold to European customers for more than **$40** per cubic meter
2. Gazprom sold its 32 percent ownership interest in a gas-producing subsidiary, Purgas, to Itera **for $1,200,** while the **market price was $400 million**
3. Itera became the world's **seventh largest natural gas company** in a span of only seven years during the 1990s.

- Each of related company's members had **family ties** with the executives of Gazprom.

- In 2001, Boris Fedorov, a former head of the Ministry of Finance, was appointed to Board of Directors and in his **5-week investigation** he uncovered evidence that Gazprom assets had been systematically transferred to the managers.
- loss of **$2 billion to $3 billion each year due to "corruption, fraud and simple theft.**

Investigations

William Browder, Hermitage's chairman, a former partner in the Wall Street, and a minority interest stakeholder, investigated that the company was **"giving away"** its natural gas reserves each year to **Itera** and other privately owned companies controlled by Gazprom executives.



After the "special audit"

PwC did not identify any "deals in which Itera benefited at the expense of Gazprom

The reports indicated that PwC's investigation had been severely hamstrung by a **lack of cooperation** on the part of both Itera and Gazprom officials

Itera's management had refused to provide documents requested by PwC auditors, while 19 executives and former executives of Gazprom, including Rem Vyakhirev, had refused to answer questions posed to them by the auditors

William Browder suggested that in the future the company report in its income statements, **"Profit after Stealing and Subsidies"** and **"Profit If Stealing and Subsidies Are Eliminated"**

1. List the challenges that a major accounting firm faces when it establishes its first practice office in a foreign country. Identify the key factors that accounting firms should consider when deciding whether to establish a practice office in a new market.

Political

- Political stability, legal and government regulations
- Accounting standards and practices applied in the country, its tax guidelines and employment law

Economic

- Tax rates, interest and exchange rates, economic growth and unemployment rate
- Future costs of the company (e.g. research and training related costs)

Social or cultural

- Ethical standards or applied normal behavior
- Cultural limitations

Distance and Time

- Significant investment in travel costs
- Time zone differences

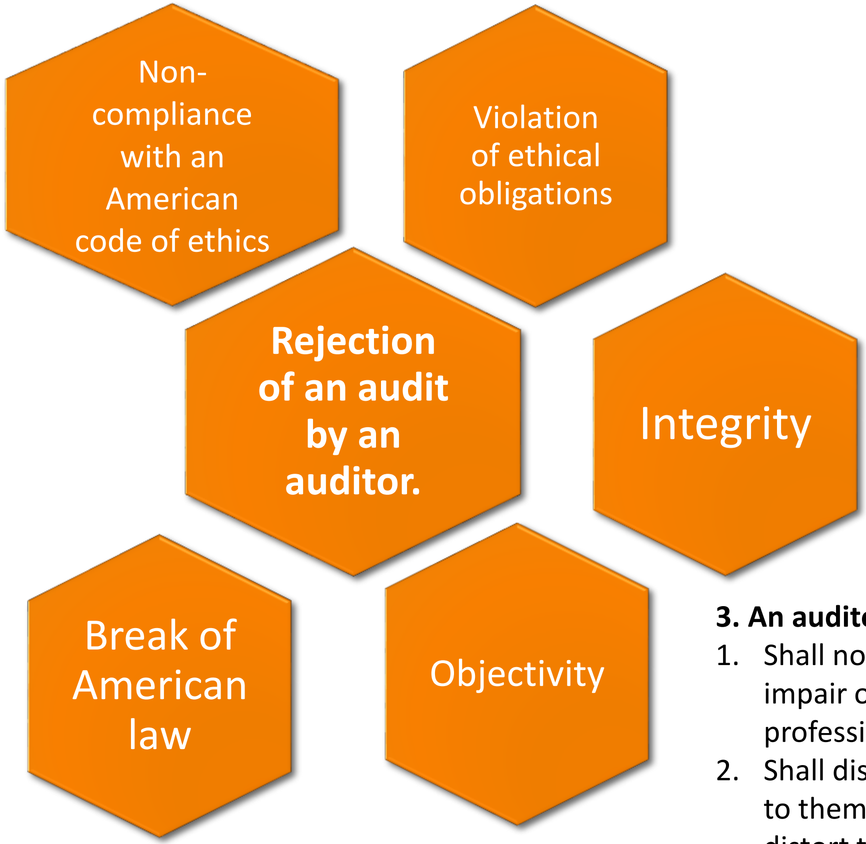
Reliable Partners or Clients

- High competition
- Local vs. international audit companies

2. Suppose that a U.S.-based accounting firm has a major audit client in a foreign country that routinely engages in business practices that are considered legal in that country but that would qualify as both illegal and unethical in the United States. What specific moral or ethical obligations, if any, would these circumstances impose on this accounting firm? Explain.

1. A US based accounting firm has to be firstly in compliance with its general **American Code of ethics**, where legal and ethical requirements have to be met by a company even if it operates overseas.

Acceptance of a client operating illegally and unethically basically means to break the law.



2. An auditor:

1. shall not knowingly be a party to any illegal activity, or engage in acts that are discreditable to the profession of internal auditing or to the organization
2. Shall respect and contribute to the legitimate and ethical objectives of the organization.

3. An auditor:

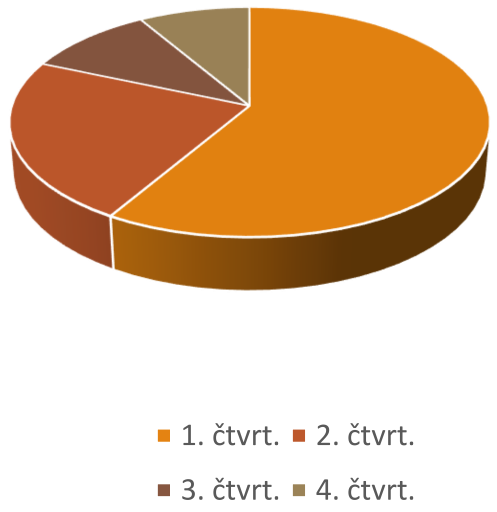
1. Shall not accept anything that may impair or be presumed to impair their professional judgment
2. Shall disclose all material facts known to them that, if not disclosed, may distort the reporting of activities under review.

3. What responsibilities, if any, do you believe PwC had to Gazprom's minority investors?

Minority investor is an equity holder of a firm **who does not have the voting control of the firm.**

Many transactions with related parties were not disclosed and there was a **lack of transparency** of PWC to the minority investors **(violation of AU316.40)**

- Credibility
- Disclosure
- Independence



- **Related transactions with Itera and other companies.**

4. In your opinion, should PwC have agreed to perform the "special audit" of the Itera transactions? Defend your answer. In your answer, identify the specific ethical issues or challenges that the engagement posed for PwC.

PwC

In our opinion, PwC should not have agreed to perform the audit of Itera's transactions. It was against their accounting ethics because they were the firm auditing GazProm for a long time before all the Itera's transactions got disguised. This would be for Pwc like they were auditing itself so it wasn't credible at all, and it is a threat of self-review. The main problem is also that PwC should have disclosed Itera as a related party in the footnotes to the company's financial statements, so it leads that the audit wasn't done properly with due care. Basically, the company lost its integrity, objectivity and independence

self-review

self-independence

objectivity

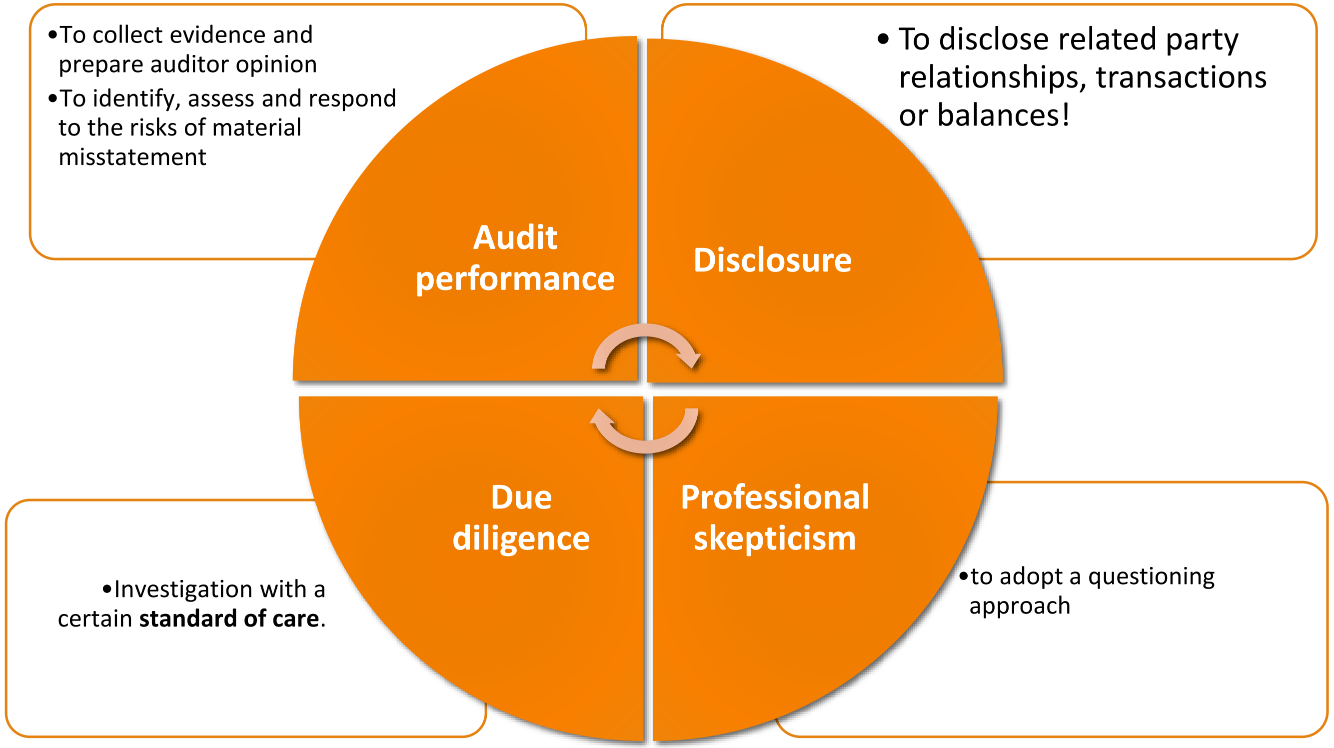
credibility lost

familiarity

Threats—

5. In the United States, what responsibility do auditors have to determine whether or not "related parties" exist for a given audit client? Explain.

Auditing Interpretations of Section AU sec. 334, Related Parties; and AU sec. 9334, Related Parties



6 Explain how the British “true and fair” audit approach or strategy differs from the audit philosophy applied in the United States. In your opinion, which of the two audit approaches is better or, at least, more defensible?

‘**true and fair**’ concept

- A part of English law and central to accounting and auditing practice in the UK, the European Union, Singapore, Australia, and New Zealand
- **Closely identified with judgement**
- **True** -- financial statements are **correct** and have been **prepared according to IFRS** and they **do not contain any material misstatements** that may mislead the users.
- **Fairness** implies that the financial statements **present the information faithfully without any element of bias** and they reflect the economic substance
- **Law** requires the auditors to expressly state in their audit report whether in their opinion the financial statements present a true and fair view.

‘present fairly in conformity with generally accepted accounting principles GAAP’

- A financial concept in conformity with GAAP, United States
- Tends to be **more rule based**
- The auditor sees financial statements **as fairly presented only if they are in accordance with GAAP**
- a very broad definition of fairness (**relative and objective viewpoint**)
- **Relative viewpoints** recognizes truth in relation to **individual circumstances, viewpoints or frameworks**.
- **Objective viewpoints** focuses on discovering of needed facts, an impossibility in the socially constructed sciences of accounting.
- The auditor should look to the requirements of the **Securities and Exchange Commission** for the company under audit with respect to the accounting principles applicable to that company.

7. In recent years, there has been an ongoing debate in the accounting profession focusing on the quality of the accounting standards issued by the International Accounting Standards Board versus those issued by the Financial Accounting Standards Board. Research and briefly explain the key philosophical difference between those two important rule-making bodies that significantly affects the nature of the accounting standards promulgated by each.

IASB- IFRS

1. IASB is funded by market participants and regulatory authorities

2. Aim is to establish **a common global language for company accounting affairs**

3. principles-based

4. objective-oriented

5.Emphasis on professional judgements

6. LIFO is not allowed method for **inventory measurement**

7. **IFRS does not consider comprehensive income** to be a major element of performance and does not include it.

8. **Intangible assets** are recognized only if the asset will have a future economic benefit and has been measured reliably.

9.A simplified version of GAAP (3000 pages)

FASB- GAAP

1. FASB is funded from fees paid by issuers

2. rules-based

3.procedure-oriented

4. Emphasis on best practise

5. Both, LIFO and FIFO are practices for **inventories**

6. Requires financial statements to include **a statement of comprehensive income.**

7. Acquired intangible assets under U.S. GAAP are recognized **at fair value**

8. Too complicated and expensive for application (app 25000pages)

GOALS of FASB and IASB is the **highest relevance, representational fairthfulness, transparency and comparability of accounting information**.

Reference

1. Case study Gazprom
2. Public Company Accounting Oversight Board, **AS 2815: The Meaning of "Present Fairly in Conformity with Generally Accepted Accounting Principles". Available on:** https://pcaobus.org/Standards/Auditing/Pages/AS2815.aspx
3. The Institute of Auditors, Code of Ethics. Available on: https://na.theiia.org/standards-guidance/mandatory-guidance/Pages/Code-of-Ethics.aspx


THANK YOU FOR YOUR ATTENTION
NOW PLEASE CLAP
memegenerator.net