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Abstract

This paper explores the differences between the Russian and western accounting systems. As western hospitality companies enter the markets of the former Soviet Union this understanding will be imperative. Under the Soviet government the hospitality industry in Russia was very poorly developed. After the collapse of the U.S.S.R in 1991 many businesses in Russia including hotels and restaurants flourished but the accounting systems to support them remained antiquated or non existent. Unfortunately, the current Russian accounting system is still closely reflecting the Soviet accounting system. Russian accounting standards are very confusing for foreign investors, creditors, and managers who want to do business in Russia.

The Soviet Way of Doing Business

In a 70 year period before the collapse of the U.S.S.R. there were little or no private businesses in Russia. Russia is the largest republic of the former Soviet Union. Most Russian businesses were owned by the government. Companies were issued so-called "achievement goal plans" that indicated production targets that companies were supposed to reach. The Russian accounting system, as part of a centralized economy was primarily focused on execution of the government-established goals.

For Russian business there was no concept of market competition, advertising or financial profitability. In fact, many companies were not profitable. Those companies that were not profitable, in most cases, were able to automatically receive a monitary subsidy from the government. This way of doing business was common for almost every production and manufacturing industry. After 1917 the Soviet/Russian accounting system was undergoing consistent changes and the main objective of those changes was to adjust the Russian accounting system to a socialistic economy. After 1991 those changes were supposed to meet standards of a country with market economy principles. Table 1 describes the main steps in the development of the Russian/Soviet accounting system.

Table 1

Main Steps in the Development of Russian/Soviet Accounting

Years	Main Steps in the Development of Russian/Soviet Accounting
1917-1918	Adaptation of accounting principles to a new stage of economy.
1918-1929	Development and implementing accounting principles that are applicable to country with a socialist system.
1929-1953	Building of socialism deformation of accounting principles.
1950s	Standardization of accounting documentation.
1960s	Development of a new accounting theory.
1950-1980s	Application of technology to accounting.
1992	Development of a completely new chart of accounts applicable to a country with market economy principles.
1998-2001	Issuing of more than 15 significant accounting regulations.

The hospitality industry in the former U.S.S.R. was also controlled and financed by the Soviet government (Papiryan, 1994). Soviet ideology encouraged domestic tourism and the Soviet government heavily promoted it. The governmental promotion of domestic tourism meant that most Soviet citizens traveled within the U.S.S.R. (Usikin, 2000). Intourist, Sputnik, and the Central Committee of Tourism and Excursions were three large governmental organizations responsible for overseeing the tourism and hospitality industry (Ryabinkova, 1999). Russian government allowed only a very small number of tourists to visit Russia, especially from capitalistic countries.

The Hospitality Industry After the Collapse of the U.S.S.R.

After the collapse of the U.S.S.R. in 1991, the Russian borders began to open which significantly changed international travel for Russian citizens but also increased international tourism. Accommodation facilities, internal transport services, restaurants and many other elements of an effective tourist infrastructure needed improvement. According to a report by Moscow's city government (1993), after 1991 the number of international tourists visiting Russia increased significantly. Only 2.1 million international tourists visited the U.S.S.R. during the 1970s. During 1991 alone, Russia had 6.2 million foreign visitors and 70% of these tourists went to Moscow and St. Petersburg during their stay (Chernishev, 2000).

Russian hospitality infrastructure visibly lacked the resources to keep pace with the increasing visitor demand. Many western companies decided to launch their hospitality products on the Russian market. The number of hotels and restaurants that cater to international guests in Russia has increased through the use of joint ventures with Sheraton, Marriott, Radisson, and Hyatt (Bard, 1991; Blalock, 1991; Gatty, 1991). These foreign joint ventures provide Russian hospitality operations with know-how and desperately needed financing and brand identification for western tourists. Many of the largest hotel brands (Novotel, Best Western, Inter-Continental, Holiday Inn, Starwood, and Marriott) are present in Russia, despite a business climate that is not always favorable.

Russia's potential for tourism growth and the current under-capacity in lodging still make Russia a very attractive market for international hospitality investment (Karhunen, 2000). The leader in the Russian market is the Marriott Corporation, with six hotels in Russia currently (www.marriott.com 2007). The largest restaurant chain in the Russian market is McDonalds. Since 1990, McDonalds has opened 103 restaurants in Russia. The success of McDonald's restaurants in Russia was the major factor in why other American fast-food chains such as Subway, Pizza Hut, KFC, and Sbarro decided to enter the market in Russia (Sagdiev, Kudashkina, & Musatov, 2003). Despite the political instability, economic uncertainty, and consumer unrest, hospitality investors see Russia as a market with much potential. According to Alon and Toncar (1999), developing countries became an attractive niche for franchising opportunities that have a high demand for well-established marketing and management practices.

Western managers, investors, and creditors who choose to be engaged in the hospitality business in Russia found some aspects of business quite challenging due to the difference in Russian and Western culture such as, social systems, governmental regulations and unfortunately, a Russian accounting system that was originally developed for a country without a market economy.

Main Points of Distinction between Russian and U.S. Accounting Practices

The U.S. accounting system consists of several branches: financial accounting, cost accounting, managerial accounting, tax accounting, auditing, and accounting systems (Schmidgall, 2006). In contrast, the Russian accounting system for many years consisted of only three branches: bookkeeping, cost accounting and statistical analysis. The last element was always included in the concept of accounting and its primary function was the implication of different statistical techniques for determination of how well a company can meet the production performance expectation of the Soviet government.

Enthoven (1999) stated that the Russian accounting system obviously has some similarities to the international accounting systems in terms of a double entry book-keeping system, balance sheet continuity, recording of assets on the basis of the original cost acquisition, general consideration of the growing concern and valuation of foreign currency using the market exchange rate.

After the collapse of the U.S.S.R. many companies were privatized and many new businesses were opened, some with the help of foreign investors. The Russian government expressed an interest in changing the Russian accounting system in favor of supporting western based accounting systems. In 1991 a new chart of accounts (Russian equivalent of uniform system of accounts) was significantly different from the one that was used under the centralized government economy. This chart of accounts was very general and was applicable to all Russian industries unless they were requested to use their own chart of accounts. Hotels and restaurants in Russia do not have their own chart of accounts and there are very few industries that do, such as commercial banks. Despite these limitations, the accounting standards that are currently used in Russia are beginning to include more concepts that are typical for the market economy such as credit liability and debit liability, deferred taxes and outstanding debt collection period which were not well-introduced to Russians. The transition however is slow, as for years Russia never paid significant attention to the service sector of the economy. This means that this chart of account may be much easier for companies in the manufacturing sector to use than hospitality establishments. Furthermore, in contrast to the U.S., Russia does not have a uniform system of accounts for restaurant and hotel industries.

Over the decades Russians were not aware of such concepts as managerial accounting: it was simply unnecessary because all planning was done on a centralized governmental level. The hospitality industry in the United States always implements new managerial accounting techniques. Such basic managerial accounting concepts as cost-profit-volume analysis, forecasting methods and capital budget are clearly included in the hospitality educational curriculum for American universities. Perhaps, it is not surprising that a study of Damitio and Schmidgall (2006) found that when managers and controllers in the lodging industry were asked to rank importance of managerial accounting skills none of the skills were rated as "non important."

Uniform system of accounts for the lodging industry (USALI) is widely recognized in the U. S. hotel sector and presents a variety of occupancy ratios. A translation of USALI in Russian may be very helpful for Russian hotel managers and accountants. Despite the fact that some of these terms may be briefly covered in the Russian educational curriculum, they do not receive as much attention as they should. Thus, many hospitality professionals in Russia cannot identify and apply those concepts to their businesses. Operating ratios that are broadly used for the American hospitality industry such as revenue per available room, occupancy percentage, food cost percentage and other similar ratios that are mentioned in USALI are not deemed by the majority of Russian accountants and managers as ratios of significant importance. Such an attitude most likely takes place because Russian accountants and managers have a lack of knowledge and expertise in terms of hospitality managerial accounting.

The current Russian accounting system uses a reporting system that is much more complicated compared with the U.S. based General Accepted Accounting Principles

GAAP-US and presents major interpretation challenges for U.S. managers, creditors and investors. The U.S. has only four main types of financial reporting: (a) balance sheet, (b) income statement, (c) cash flow statement, and (d) owner's equity statement. The Russian financial reporting system consists of several parts: (a) balance sheet, (b) report of financial results (a form similar to the US profit and loss statement), (c) report on capital flow, (d) report on cash flow, (e) attachment to a balance sheet disclosure note, (f) the summary of audit report and additional possible forms that a company may be required to have depending on the nature of the business. The Russian government requires preparation of multiple forms that are complicated, time-consuming and very difficult to comprehend for a person who is only familiar with western accounting systems.

According to Zaiko (2002), the main challenge that Russian accounting may present is the ability of management to avoid a presentation of the objective financial position of a company. Russia was well-known for its so-called "black" accounting system which helped to hide the real amount of profits a company was making, and as a result, significantly reduced the amount of taxes the company owed. It is used in Russia to a much larger extent and is more prolific than in the U.S. The official accounting forms could be filled out correctly and present, from a first glance, information that makes sense but might not necessarily be reliable information. Perhaps many foreign businessmen have to face the reality that they simply can't trust this sort of accounting information. Despite the fact that many Russian companies are ready to discuss strategy and financial goals, their accounting information still doesn't have high levels of transparency. Russian businesses still manage to successfully hide monies in off-shore banks and such actions are misleading for the western investors.

In contrast to the United States, Russian hospitality businesses have internal control challenges as they have adopted creative ways of not paying taxes that in many cases is simply illegal. For example, a basic transaction, such as the payment for a hotel room or meal, may not be recorded in Russian hotels, to avoid the payment of taxes. As Russia does not have a well developed system of credit cards, checks or money orders, the majority of payments by individuals are made in cash. Therefore, managers or assistant managers can easily deposit the cash directly in their pockets. In some cases they can issue a guest a receipt, but the guest may not necessarily choose to keep a copy of their receipt for their records. Another common practice of doing business in Russia is to pay invoices for services provided by a fictitious (non existent) company. Even in cases where business is conducted with a legitimate company, invoices may be inflated and the incremental amount pocketed by the Russian Hotel Manager. These instances may occur more frequently in the case of capital expenditure payments such as bathroom renovations. Small hospitality establishments that are not affiliated with international chains in many cases pay salary to their employees in cash but their records show much smaller amounts than what they are actually paid. The main reason for doing this is to avoid paying taxes which are similar to American Federal Insurance Contributions Act (FICA) and Federal Unemployment Tax Act (FUTA). The preceding examples of, business transactions are pervasive through most businesses in Russia and not unique to the hospitality sector. Expatriate managers preparing for a hotel assignment in Russia should be prepared to come across these business practices and lapses in internal control that under report revenues and profits. In this particular situation a high level of trust in Russian managers, accountants, and controllers may not be always beneficial for business prosperity and a proper presentation of financial results.

Due diligence is a form of examination that can be provided by foreign audit companies that do business in Russia. It is a beneficial tool for determining if a hotel or restaurant should be purchased and for how much. On the other hand, if a business is purchased and some uncommon accounting practice is going to be implemented, investors and creditors are not going to get the same results as they expected after the due diligence report.

The Russian accounting system doesn't utilize logical principles and the forms have conflicting information or redundant information. Many forms have questions that are confusing and can be answered differently based on subjective interpretations of individuals who fill out those forms. One reporting form doesn't distinguish between net income and undistributed profit and assumes that those two terms are absolutely the same. These conflicts may cause Russian companies to face problems with tax authorities if they even make a small deviation from the standard reporting system.

The materiality concept that is widely accepted in international accounting systems doesn't exist in the Russian accounting practice at all. In the U.S. accounting system, if the cost of an item really doesn't have an impact on decision making, it doesn't have to be treated under GAAP regulations. A purchase of a $20 calculator will be classified as an expense immediately even if its useful life is estimated as five years. All items and events even if they do not "really make a difference," should be recorded very carefully. Failure to conduct such recording can bring substantial penalties for a violation of accounting standards and regulations.

The Russian accounting system doesn't properly reflect technological changes that take place in a modern environment. For example, Russian companies are still required to keep all documentation in a paper format and not allowed to keep it in any electronic format as foreign companies do. That gives an immediate impression of old-fashioned bureaucracy.

Russia is not the only country in the Former Soviet block that is making an attempt to adopt western accounting standards to its benefits. Other Eastern European countries such as Romania, Poland, Bulgaria, Croatia and others have started to make a transition to a new accounting system and currently stand on different levels of development (Zeghal and Mhedhbi, 2006). According to Bailey (1995), those countries face quite similar problems as Russia does in terms of adapting their business to western accounting standards. Those problems include unsteady economic conditions, poor legislation, possible hyperinflation, complicated financial reporting and a lack of local accountants who have a good knowledge of western accounting standards.

U.S. managers who may consider doing business in Russia may find out that a variety of accounting operations are done very differently under Russian GAAP in comparison with U.S. GAAP. Many Russian businesses pay more attention to filling in all forms correctly and prefer a correct form approach over reliable substance. There are a variety of differences between U.S. GAAP and Russian GAAP. For example, the Russian accounting system has a very limited number of exemptions for small businesses and even a small restaurant or bed and breakfast has to deal with extensive documentation; depreciation may not necessarily be calculated in certain cases when a building is being restored; all intangible assets are amortized and can not be revaluated; a lack of guidance on reporting offsetting cash in a cash flow statement; cash equivalents are not considered as a part of cash and changes in cash; and, revenue from sales is recognized when the legal title passes, just to name a few. Balance sheets and income statements have a relatively strict format that is supposedly followed by all business establishments and can not really be customized for a hotel or restaurant. They also present a historical cost despite a very high level of inflation in Russia. Russian GAAP is similar to U.S. GAAP and consists of three parts: investing, financing, and operation activities. However, there is no proper guidance on classification of included items, deposits may be considered as an investment activity, and there is no concept of indirect methods when it comes to the conversion of net income to net cash flow.

Some Light at the End of the Tunnel

In the last several years some Russian companies, especially those who have foreign capital or interest in the attraction of foreign capital, started to prepare their financial documentation not only based on Russian accounting standards but also based on foreign accounting standards. However, they always have to prepare financial reports based on Russian regulations and preparation of reports based on foreign accounting standards can only be see as an addition. Russian enterprises may basically choose between two main accounting standards: GAAP-US and International Financial reporting Standards (IFRS) (formerly called International Accounting Standards (IAS). American-based hospitality companies that introduced their products and services to the

Russian market use GAAP-US in addition to Russian accounting standards. Both of these accounting standards have a theoretical framework that regulates how financial information should be recorded and how financial reports should be prepared. Despite the fact that these two standards have some similarities of course there are some differences. Peter Holgate, Senior Technical Partner at PricewaterhouseCoopers, believes that one day IFRS and GAAP-US will become sufficiently joined but it may take some time. For example, a U.S. balance has to be presented in decreasing order of liquidity. Under IFRS regulations it is not necessary unless a company believes that such order of presentation will provide more relevant and full information. A U.S. income statement may be presented in either single step or multiple step format. IFRS demonstrates much more flexibility with income state format.

According to McGee and Preobragenskaya (2006), today's managers have two reasons for implementing western accounting systems. First, Russian managers need information that will help them make effective decisions that an old system may not necessarily be helpful with. Despite the fact that there are still significant gaps in knowledge about managerial accounting, there is already some interest in this topic. Second, in order to attract western capital and capture attention of foreign investors and creditors, financial documentation has to be presented in a format that would be easily understandable by international shareholders. Ironically, 57% percent of Russian accountants believe that their own financial statements do not provide a true picture of their company's financial position and 71% of accountants believe that those statements do not reflect accurate economic reality (Rozhnova, 2000).

Implications and Recommendations

The primary reason for this paper is to prepare American hospitality managers, creditors, and investors for the realities of the Russian accounting system. Due to specific features of the Russian accounting system, Russian enterprises and joint-ventures can't always easily apply western accounting standards. In the last several years Russian accountants and managers started to express a clear interest in learning about GAAP-U.S. and IFRS. However, despite the high demand, there are still a very limited number of professionals who have substantial knowledge of both Russian accounting and international accounting systems.

Russian universities and educational institutions do not have sufficient personnel who can teach the standards of international accounting. Many faculty members received their degrees under the former Soviet Union and only have knowledge of the "old accounting system." Those faculty members, who have received their education recently, perhaps could have a very limited number of courses in international accounting, but it still doesn't give them sufficient expertise for teaching these courses.

It may be helpful in such cities as Moscow and St. Petersburg to have more centers that will train individuals in international accounting and have full-time instructors who can provide classes based on a high level of demand for such knowledge. It would be very beneficial for Russian accountants to take courses that introduce them to new ways of doing accounting. Providing them with a standardized test (similar to American CPA) may help to make an assessment of their expertise in accounting issues.

Russian universities and training centers often rely on foreign textbooks to teach international accounting. An accurate translation of those books can be quite a challenging assignment because a person who can translate those books not only needs to have a very high level of linguistics expertise but also be familiar with accounting. As an additional concern, despite strong academic preparation in foreign languages, Russian translators are not always able to understand Western business concepts due to differences between the capitalistic and socialistic economic system.

In the last several years, a variety of business training programs became very popular in Russia. Russian institutions would benefit by bringing faculty members from western institutions of higher education to provide them with intensive courses related to international accounting. This investment in faculty training and education in international accounting has the potential for raising the caliber of accounting education and practice in Russia.

Regulation of accounting standards in Russia should be implemented by professional accounting organizations and not the government. Such an organization should first pursue interests in the development of fair accounting systems under conditions of the market economy and not bureaucratic interests of the government.

Perhaps American businessmen, before trying to make serious business plans in Russia, should seek out individuals who can make proper comparisons between U.S.-GAAP and Russian accounting standards. Each profession has its own specifications and working with individuals who may understand the nature of hospitality operations from both American and Russian perspectives is a valuable attribute.

Today the majority of hospitality establishments rely on the Big Four accounting firms for preparation of their financial reports. Despite the fact that their services are quite expensive, international businesses that are serious about attracting foreign capital believe it is worth paying the price for their services. Those companies that made their presence very clear in the Russian market after the collapse of the former Soviet Union not only have a sufficient number of foreign employees but also invest time resources in local populations in order to prepare them for quality work.

Foreign businessmen should understand that the Russian accounting system can not be converted to international standards within a short period of time. It will be a slow but consistent process. The Russian accounting system should properly correct disadvantages of the current accounting system and properly reflect changes that take place on the Russian market.

Russian accountants and managers do not have proper professional judgment and focus more on following proper directions on their financial reporting. Such development simply took place because for many years the Russian accounting system was primarily trying to satisfy the government and tax services in contrast with the U.S. accounting system that was more focused on creditors, investors, and managers. The main purpose of Russian accounting reports is not to present objective and truthful representations of the financial position of a company. It is more concerned about meeting all government regulations and procedures. International accounting standards should continue to focus on the presentation of information that is relevant and significant for the description of a company's financial matters and not extensively focus on putting information in their reports even if it is not very "helpful"; something that many companies are still doing.

The hospitality businesses in Russia may specifically suggest developing regulatory accounting standards that can help regulate accounting activities and reporting.

This initiative should be undertaken by industry professionals who understand the nature of hospitality operations.

There may be a team of American-Russian authors who develop a manual on the Russian accounting system that can be used as a reference point for Americans who want to develop hospitality businesses in Russia.

Some Russian accountants who have already learned more about U.S.-GAAP do not have literature that focuses specifically on the hospitality industry. Translating well established hospitality accounting textbooks used in the west will further help students, faculty and industry professionals in Russia.

Russian educators should include courses on international accounting in their curriculum especially for those majors who actually specialize in accounting. Introducing students to international accounting early in their curriculum will help them and their businesses in Russia.

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