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**THE APPLICATION OF IFRS IN  
AZERBAIJAN**

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Initially, I would like to thank to my scientific supervisor, PhD candidate Polad Azizov for his advice, encouragement and patient guidance. I am extremely lucky to have a supervisor who cared so much about my work and responded my questions so promptly.

# **ABSTRACT**

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The application of International Financial Reporting Standards in Azerbaijan has been discussed by the professional community in recent decades. Discussions in this area do not cease to this day. Experts agree that these standards have already penetrated into the business environment of our country and are "embedded" in the system of regulation of accounting and reporting at the state level.

The process of unification of accounting is directly connected with fundamental changes in the world economy as a result of international integration and internationalization of economic activity. The transition to market relations, the emergence of international economic and financial ties put forward a number of topical issues on improving accounting and its approach to international standards. In the west, accounting and reporting in Azerbaijan do not meet international standards, concepts, postulates and accounting principles, generally recognized in Western theory and practice. At the same time, it is difficult to find at least one country in the world that has built its national accounting system, based entirely on international standards only. However, this does not mean that countries should not seek to develop them; international accounting standards should be a trade-off between the characteristics of national accounting schools in those countries whose representatives are involved in their development.

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## INTRODUCTION

The development of market relations and the lack of financial resources stimulate the process of creating large corporate structures with the goal of pooling capital and increasing attractiveness for external investors.

To increase the interest on the part of foreign investors, a universal language of communication is required, which can reliably inform the information on the financial condition of the company, that is the language of accounting. Accounting is a cartography of finance and on how fully and clearly it is composed, the degree of reliability of the received idea about the financial position of the company depends. To increase the universality and transparency of accounting, it is necessary to unify it according to certain standards. The system of International Financial Reporting Standards, which summarized the existing accounting principles and standardized them in order to increase the reliability and transparency of financial reporting, was recognized as the means for unifying accounting.

The government of the Republic of Azerbaijan has developed a program according to which all socially significant enterprises until 2010 are obliged to make a transition to an international system for the provision of financial reporting. The transition to IFRS should give the development of the economy an additional impetus, promote transparency and attractiveness of Azerbaijan enterprises. There are several ways to obtain financial statements in the IFRS standard, the most common of which is the way of transforming data prepared in national standards, which is inherently a laborious process. To transform data, it is necessary to develop a methodology, by painstakingly studying all the tricks of international standards or by attracting relevant specialists who are still very few in the modern labor market and the cost of corresponding resources is quite significant.

# **CHAPTER I. COMPOSITION, STRUCTURE AND PURPOSE OF INTERNATIONAL FINANCIAL REPORTING STANDARDS**

## **1.1 Prerequisites for International Financial Reporting Standards**

International financial reporting standards are aimed at achieving uniformity of accounting practices that will allow accounting to be used as a universal business language. The trend towards the globalization of capital markets has led to the need to bring together existing accounting practices. Before the Second World War, all funding needs were met from internal sources. However, after the war the situation changed. This was facilitated by special economic programs to restore the destroyed countries, which ultimately led to a significant increase in international capital markets. Currently, there are well-known capital markets such as Eurodollar, Eurocurrency, and the Asian Dollar, in which companies from the United States, Japan, the United Kingdom and other developed countries are represented. The interdependence of capital markets is confirmed by such phenomena as the stock market crises of 1987 and 1998, affecting virtually all the leading markets in the world.

The ancestors of accounting are considered to be the Italian city-states of the 14th-15th centuries who distributed the "Italian method of double-entry bookkeeping" first to the rest of Europe and then to the whole world. Since the XIX century, the development of accounting theory and practice was significantly influenced by England and Scotland. Nowadays the USA plays an increasingly important role in the field of accounting. Organization, technology and accounting concept as a variety of goods are exported and imported around the world, providing a semblance of accounting systems in different states.

Initially, accounting systems of different countries differ significantly. The main reasons for the differences are:

- socio-economic factors;
- political factors;
- geographical factors.

### *Socio-economic reasons*

As socio-economic reasons, the following are distinguished: the nature of development of capital markets, the number of investors and creditors, participation in international capital markets, the level of inflation, the size and organizational structure of enterprises, the overall level of education.

Countries are divided into high-level and low-inflation countries. The former include the countries of South America, Africa, and also Azerbaijan. For these countries, the financial statements are adjusted to inflation indices. For countries with a low level of inflation, this problem is not relevant.

Due to the high level of economic development in the United States, the United Kingdom, the Netherlands, Germany and other developed countries, enterprises are quite large and complex organizational structure, the level of education in these countries is also quite high. This leads to the complexity of accounting information, which, on the one hand, adequately reflects the existing economic reality, and on the other hand, is adequately perceived by the user. In underdeveloped countries, accounting systems are simple because of the small size of enterprises.

### *Legal system*

The next factor that determines the essential differences in the financial statements of different states is the legal system. Depending on the type of legislation and the degree of state influence on various aspects of life, most countries can be conditionally combined into two groups:

- Countries that have legislation of general legal orientation;
- countries with ramified (extensive) codes of laws.

In the states of the first group, the laws, as it were, point to the limits within which individuals and legal entities have freedom of action. This common law system was originally formed in the UK and is present in many countries that have traditionally close ties with it (federal law of the USA, the legal system of Ireland, India, Australia and some other countries). The activities of companies are not regulated in detail, nor are the rules for preparing and publishing financial statements. Accounting standards in these countries are not regulated by the state, but are determined by various professional organizations of accountants.

In the countries of the other group, legislation is based on Roman law. This legal system stipulates laws of a strictly deterministic nature, individuals and legal entities must follow the letter of the law. Most countries introduce into the law rank and accounting standards. All activities in the field of accounting are detailed and fairly rigidly regulated. The main task of accounting in such countries is the calculation of state taxes and control over their payment. Such countries include Germany, France, Argentina, and others.

#### *Influence of other countries*

The influence of the accounting rules of one country on the accounting rules of another country may be due to political or economic dependence, geographical location.

International accounting practices are not uniform. There are international, regional and national accounting standards. National standards are developed by each country independently. At the regional level, the comparability of reporting is regulated by both professional accountancy organizations and other



organizations. For the member states of the European Union (EU), the problem of harmonization (harmonization) of accounting has been reflected in the EU directives.

A compilation of the European accounting methodology is carried out by the Federation of European Accountants (EU), and the practical implementation of the directives is the EU Contact Committee.

In the international practice, several accounting systems are common, but they are not originally intended to regulate accounting and reporting in individual countries. Accounting in any enterprise is influenced by the specific characteristics of each country and represents its national system.

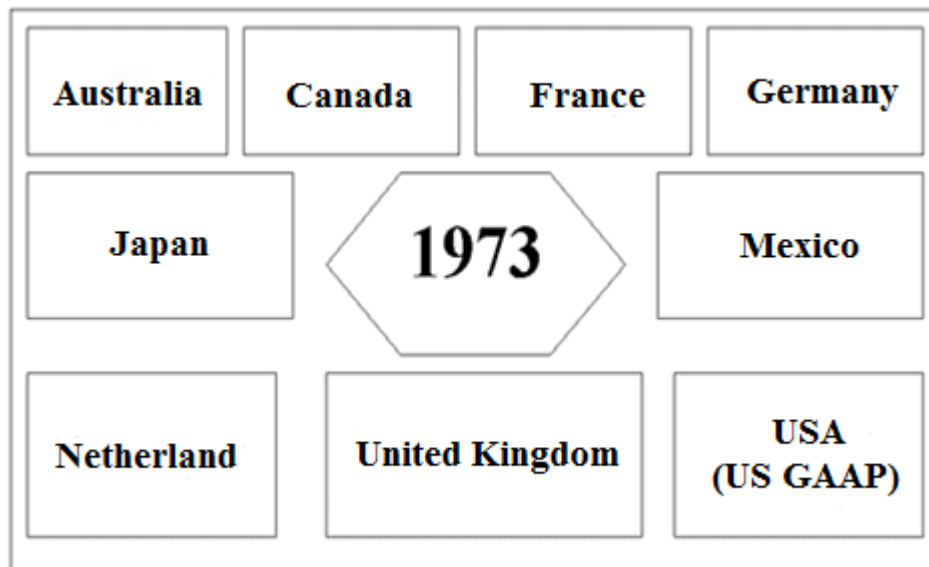
The purpose of the development of international standards and their use is the harmonization of national accounting and reporting systems in the direction of improving the consumer characteristics of the company's financial statements.

## **1.2 Composition and structure of International Financial Reporting Standards**

The UN Center for Transnational Corporations has started work on the International Financial Reporting Standards. For the growth of global economic relations, a universal language of communication was needed.

The International Accounting Standards Board (IASB), or the International Accounting Standards Committee, was established by professional accounting organizations in a lot of countries as an independent body of the private sector in 1973. (Pic.1.1)

### **(Pic.1.1) The founders of the International Accounting Standards Board**



Since 1981, the IASB has been fully autonomous in the implementation of International Financial Reporting Standards and in the discussion of documents related to international accounting.

Since 1983, members of the IASB have become all professional organizations - members of the International Federation of Accountants (IFAC).

The end of the year 2000, the IASB included all professional accounting organizations (over 140) that are members of the International Federation of Accountants (IFAC).

The International Accounting Standards Board (IASB) was created in April 2001 to replace the International Accounting Standards Board (IASB).

In the process of standardization and unification of accounting, the main role is played precisely by the IASB, although there are other organizations dealing with this same problem. They include:

- Intergovernmental Working Group on International Standards in Accounting and Reporting at the United Nations;

- Working group of accounting standards of the Organization for Economic Partnership and Development.

Thus, the Council on International Financial Reporting Standards is an independent organization whose main goal is to achieve uniformity of accounting principles.

The objectives of the Council's work on international financial reporting standards are defined in its Charter:

- It is in the interest of the public to formulate and publish standards accounting for their use in the process of financial reporting, as well as ensure their acceptance and implementation throughout the world;
- to carry out a common work to improve and unify rules, standards accounting and procedures relating to the preparation of financial reporting.

The governing body of the IASB is the institution of the IFRS trustees.

Trustees (or trustees) appoint members of the IASB, the Standing Interpretations Committee (IFRIC) and the Standards Advisory Council (SAC). Trustees also monitor the effectiveness of the IASB, seek funding, approve the budget of the IASB and amend the charter.

\* **The Council for International Financial Reporting Standards** is the main body within the structure of IFRS that is responsible for the adoption of International Standards. The Board consists of persons who prepare and use financial statements, auditors and researchers, a total of 14 members, 12 of whom work on an ongoing basis. Members of the IASB are appointed by the trustees for a term of 3 to 5 years. Several members of the Board are directly responsible for coordinating work with bodies setting national financial reporting standards. The daily work of the Council is carried out with the participation of a variety of technical and administrative personnel. The IASB

prepares and publishes IFRS, prepares and publishes the Draft Standards, establishes the procedure for reviewing comments received on published Draft Standards for discussion, publication of the basis for drawing conclusions.

\* **The Standards Advisory Council** is a forum for organizations and individuals wishing to participate in the discussion of methodological and other issues related to the application and formulation of standards, as well as in developing recommendations to the Council and Trustees on the agenda and priorities.

The Standards Advisory Council consists of 45 members appointed by the Trustees for 3 years, representing different geographic regions and areas of activity. The Advisory Board holds at least 3 open meetings with the IASB per year.

\* **The International Financial Report Interpretations Committee** was established in April 1997 to provide conceptually verified and practicable interpretations of IFRSs on emerging issues in financial statements that are not specifically addressed in IFRS, and where there are or may be unsatisfactory or conflicting interpretations in the absence of official explanations, as well as to interpret disputed issues related to the formation of financial statements.

### **The process of developing International Financial Reporting Standards**

To date, there are 41 standards (Appendix 1).

Structure of International Financial Reporting Standards:

purpose of the standard, scope and object of accounting - the definition of the accounting object and the basic concepts associated with this object;

recognition of the accounting object - a description of the criteria according to which the object relates to different elements of reporting;

valuation of the accounting object - the rules of application of the methods of assessment of various elements of reporting;

reflection in the financial statements - disclosure of information about the object of accounting in the financial statements.

The process of developing international financial reporting standards is presented in Pict.1.3:

1. STAGE - Formation of the Drafting Commission
2. STAGE - Development of draft IFRS
3. STAGE - Preparation of a working draft of the provisions of the standard
4. STAGE - Approval by the Board of the working draft
5. STAGE - Drawing up an IFRS development plan
6. STAGE - Preparation of the draft IFRS

*Pict.1.3. IFRS development process*

Standards are issued after passing strictly enforced procedures. Until the final version of the standard is received, documents for discussion - Discussion Documents and preliminary drafts are issued in order to receive comments and suggestions. Standards are issued after detailed discussion and consultation.

Discussion Paper is compiled to describe the issue, the scope of the project, and to discuss research results, provide alternative solutions to the issues discussed, the arguments and the consequences of each of the alternatives.

Stage 1 - the formation of the drafting committee. The commission is formed of specialists from at least 3 countries. The drafting committee may also include representatives of other organizations, experts in a certain field.

Stage 2 - development of the draft standard. The Drafting Committee outlines a work plan for the project, then carefully studies the practice of accounting for this issue in various countries, including various accounting techniques suitable for different conditions. Based on the results of the study, a general plan for the development of the draft International Financial Reporting Standard is submitted for consideration.

Stage 3 - preparation of a working draft of the provisions of the standard. During this stage, which usually lasts about 4 months, the drafting committee prepares the Draft Statement of Principles or another discussion paper. It formulates the basic principles for the preparation of the next document - the Draft International Financial Reporting Standard, and proposes alternative solutions and arguments in favor of adopting or rejecting them. All interested parties have the right to submit their comments and suggestions to the working draft. In certain cases, even before the Draft Statement of Principles, the Board may propose an item for discussion.

Stage 4 - approval by the Board of the working draft provisions of the standard. After considering all the comments on the Working Draft provisions, the drafting committee shall agree on its final version and submit it for approval by the Board.

Stage 5 - drawing up a plan for the development of an international standard. The Drafting Commission is drafting an International Financial Reporting Standard, which, after approval by two thirds of the Board, is usually published, and all parties may submit comments and suggestions. This stage can last from one to three months.

Stage 6 - preparation of the draft international standard. The editorial committee reviews all comments and submits the draft for consideration by the Board. For the adoption and publication of the new standard, 12 votes of the members of the Management Board (out of 16) are required. Otherwise, the Board may decide to hold additional consultations and make the necessary changes to the project. In practice, this requires the drafting of a new draft IFRS.

### **1.3 Principles of International Financial Reporting Standards**

International standards are based on two basic principles:

1. The principle of accrual means that business transactions are reflected at the time of their commission, and not as cash is received or paid. Thus, transactions will be accounted for in the reporting period in which they occurred. This principle provides an opportunity to obtain objective information about future liabilities and future cash flows, that is, it allows to predict the future results of the enterprise. The possible non-receipt of part of the announced cash receipts can be corrected by the timely accrual of the provision for doubtful debts by reducing the financial results of the reporting period.

2. The principle of continuity of activity assumes that the enterprise will continue its activity in the near future. And since the enterprise does not intend to reduce the scale of its activities, its assets will be reflected at the original cost without taking into account the liquidation costs.

## **CHAPTER II. PRINCIPLES FOR THE PREPARATION OF FINANCIAL STATEMENTS IN ACCORDANCE WITH INTERNATIONAL STANDARDS**

### **2.1 Users of financial statements**

Financial reports are general-purpose reporting documents, since they are published for a wide audience of users and are "external", as they are presented to foreign users. The ideal of the financial statements is to ensure information about the financial position, performance and changes in the financial position of the company, which is useful to a lot of users in making economic decisions.

Financial reporting documents are the most effective way of periodically submitting to the parties directly not participating in the company's activities information that is collected and processed by the accounting system.

The full set of financial statements, in compliance with IFRS, involves the following components:

balance sheet;

Profits and Losses Report;

a report showing all changes in equity;

a statement of cash flows;

accounting policy and explanatory notes.

Due to a possible conflict of interests between the managers of the company that are required to submit financial statements and external users, such as investors and creditors, reporting documents to enhance their credibility are often subject to independent audit.



Financial reporting is compiled and submitted to external users by many companies around the world. Although these financial statements may seem similar to each other, they still have certain differences, which are due to various social, cultural, political and economic conditions of the country's development. The form and content of financial reports are also affected by its users.

There are two main groups of users of accounting information:

internal users;

external users.

In turn, the data of the group of users of accounting information are divided into three categories:

- those who control the subject;
- those who are outside the subject, but have direct financial interests;
- those who have an indirect financial interest in the activities of the subject.

The category of users with direct financial interest include:

- real and potential investors;
- real and potential creditors;
- customers

The category of users with indirect financial interest include:

- tax authorities;
- Regulatory bodies;
- statistical bodies;

- other groups (auditors, consultants, consumer groups, etc.)

The consumers of financial statements are: investors, employees of the company, creditors, suppliers and other creditors, buyers, government and government bodies, the public.

They utilize financial reporting to meet their information needs. Needs arise:

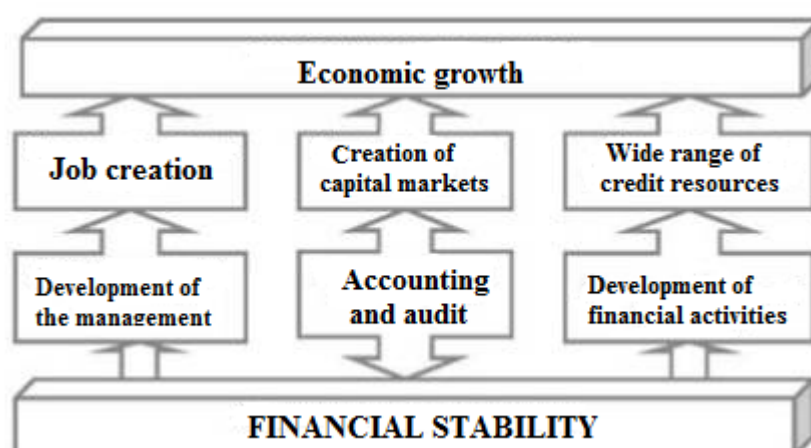
- investors in connection with the risk related with the investment.
- They need information that will enable them to assess the skill of the entity to pay dividends.
- from creditors interested in information that will enable them to determine whether loans and interest due to them will be pay on time.
- from suppliers and other trade creditors interested in information that will enable them to determine whether the amount be bound to them will be paid on time.
- buyers interested in data about the continuity of the entity, particularly when they have a long-term agreement or are subordinate on the subject.
- from employees interested in information on the constancy and profitableness of the activities of the entities. They are also interested in data that enables them to assess the subject's ability to provide them with wages, pensions and the possibility of further employment.
- from the government interested in information about the allocation of resources and, consequently, the activities of the entities. They also need information to adjust the activities of the subjects, determine the taxation policy as the basis for determining national income and other statistics.
- from the public, as actors can make a significant contribution to the suburban economy in a different ways, including employment of the population and support of local suppliers. Financial reporting can help the public by

providing it with information on development trends and recent advances in improving the welfare of the subjects.

## 2.2 The benefits of IFRS/IAS application

Integration processes in Europe and other parts of the world lead to a gradual unification of the document circulation in these countries, including financial ones. The quality of accounting and the state of professionalism aud. This can affect the economic prosperity of the enterprise.

*Pic.17. The influence of the quality of accounting on the activities of an enterprise*



Today, thanks to the joint efforts of developed countries, the Unified Accounting System is gradually being created. Therefore, IFRS today is a promising accounting system in the direction of mass substitution, introduction and use by enterprises of various developed countries of the world.

There are compelling reasons, gradually pushing towards the transition to a unified accounting standard. First, in order to avoid accounting chaos, when one enterprise generates reporting on some national and local requirements, the requirements, in turn, can confuse investors, creditors and other information users. Secondly, there will be immediate advantages for capital markets, which

will allow us to react more quickly to fluctuations or changes in information, and thirdly, it will help accountants in the formation of an early, truthful, reliable information.

International standards are widely used throughout the world. There are several levels of their application:

about the application. IFRS as national standards (for example, countries such as Cyprus, Kuwait, Latvia, Malta, Pakistan, Tobago, Thailand and Croatia);

National organizations for the development of financial reporting standards use. IFRS as a reference point for developing their own standards (most developed countries and the growing number of developing countries and countries with economies in transition, for example, Brazil, India, Ireland, Lithuania, Mauritania, Mexico, the Netherlands, Norway, Portugal, Singapore, Slovenia, Greece, France, Switzerland, etc.);

stock exchanges and regulators that bind or allow companies to provide consolidated reporting in accordance with. IFRS (among them almost all leading exchanges in the world: New York Stock Exchange, NASDAQ, London, Tokyo, and Frankfurt stock exchanges - only about 70 stock exchanges from 50 countries worldwide);

Supranational organizations, for example. European Union, announced the introduction. IFRS since 2005 for companies whose shares are quoted in international stock markets, some organizations use their funds. IFRS when compiling its accounts (International Organization of Securities Commissions, International, Olympic Committee, OECD and many others);

many financial institutions (European Bank for Reconstruction and Development, IFAC, World Bank) already carry out lending only when reporting according to. IFRS, speaking :: present. The EBRD has audited the

annual financial statements prepared in accordance with. IFRS; maintain a certain level of financial ratios calculated using data. IFRS is adequately respected by the cost accounting, accounting and information management systems, accurately and accurately reflects the financial position of the company and the results of its activities.

In most countries. Eurasia reforming accounting systems began slowly and was not always pragmatic and logical. For example, in. Kyrgyzstan the new national standards were developed on a stage-by-stage basis, including the study of several variants of their principles. This process began with the adoption of a simplified version of the standards used in the sphere of the planned economy, which subsequently were replaced by national standards based on. International Financial Reporting Standards. After the adoption of these standards came into force. Law on Accounting. But the country lacks new standards, and will expand the practice of disclosure, accessibility and transparency of reporting.

Using. IFRS for the reporting of local enterprises whose shares are listed in the levels of mandatory use on the territory of countries are shown in Table 111

In Azerbaijan, the International Financial Reporting Standards are fully adopted and accounting is developed on the basis of self-regulation. Companies are required at the legislative level to provide financial statements in accordance with international accounting principles.

Table 111. USE OF IFRS FOR ENTERPRISES IN THE LISTING IN DIFFERENT COUNTRIES OF THE WORLD

<i>Levels of application of IFRS</i>	<i>Countries</i>			
I IFRSs are not	Argentina	Indonesia	Malaysia	Taiwan

permitted by local enterprises	Azerbaijan Bangladesh Benin Fonda Vietnam India	Iran Canada China Colombia Cuba Mali	Nigeria Pakistan Serbia Syria USA	Thailand Togo Tunisia Uzbekistan Japan
II IFRSs are allowed for local enterprises	Aruba Bermuda Bolivia Gibraltar Zambia	Zimbabwe Cayman Islands Laos Lesotho Maldives	Morocco Mexico Mozambique Paraguay El Salvador	Turkey Uganda Switzerland Sweden Sri Lanka
III IFRSs require for a certain category of local enterprises	Belarus Israel Russia			
IV IFRSs require for all local enterprises	Australia Austria Bahamas Barbados Bahrain Belgium Bosnia and Herzegovina Bulgaria Brazil since 2010 United Kingdom Venezuela Haiti Guatemala	Honduras Hong Kong Greece Georgia Dominican Republic Ecuador Estonia Egypt Ireland Spain Italy Jordan Kazakhstan Kenya Kyrgyzstan Costa Rica		
There are no stock exchanges	Albania Guam	Yemen Samoa		

Other countries. Eurasia adopted national accounting standards valid on International Financial Reporting Standards or have modified their accounting standards on the source of the latter, as a rule, the state represented by the Ministry of Finance. According to experts, in most countries of the region the process of certification of accountants is significantly different from the

requirements. International Federation of Accountants, and financial reporting on methodology - tax reporting.

In practice, some enterprises in Eurasia have previously reported in accordance with International Financial Reporting Standards, but in many cases the transition of joint stock companies to new standards of art began only in 2000. Traditionally, enterprises were accountable exclusively to the state, in particular to the tax administration. In some Eurasian countries, the finance ministries still require companies to lose accountability in the traditional form, which makes them actually maintain a double-entry bookkeeping system.

Users of accounting information were mainly controlling bodies. At that time, banks formally performed their functions, they were the institutions through which the state distributed the funds. Banks would also not be interested in making a profit, because they were also public. Thus, their financial statements were also of little interest. For the same reasons ordinary people were not interested in information. The old accounting system was not intended for general use for the purpose of analysis. The financial analysis of the enterprise was limited to the comparison of the planned indicators, normative ones, and these figures were fulfilled by them and the directors of the enterprises were satisfied.

At the analysis. IFRS should be noted that this is a flexible, mobile system that positively influences the qualitative principles of Azerbaijan accounting and the improvement of national accounting and financial viability and the integration of the state into the world community.

International accounting, in contrast to the Azerbaijan, for many years served another economic system, namely, market. It is known that in a market economy, the activities of enterprises are focused on profit and enrichment of business owners, and accounting is carried out, first of all, in the interests of business owners. Main advantages. International state of accounting standards:

clearly determines the property status of the owners of the enterprise;

accounting is carried out not only for the sake of securing the fixing of economic operations, the property of the enterprise, it allows you to monitor the fulfillment of obligations by the enterprise, the availability and movement of property, the effective use of material and financial resources

allows to carry out an effective financial analysis of the enterprise for its liquidity and solvency;

gives an opportunity of a real forecast concerning the future activity of the enterprise;

financial statements prepared under IFRS are available not only for specialists, but also for a wide range of users.

The ability to compare ourselves with competitors and companies that produce similar products provides additional benefits. Companies will understand that with their own financial statements, you can get additional information, on the basis of which you can see how this reporting differs from others. It will be possible to provide useful information on comparing your own data with those of competitors in other countries. This information will be a significant help in making managerial decisions.

The main prerequisites for the need to transition to IFRS:

the expansion of both vertical and horizontal economic ties has led to the enhancement of the independence of economic entities, which, in order to make decisions, need qualitative information, fully and truly reflects all economic processes;

the activation of the role of money has led to an increase in the need for credit funds for which banks require from the subjects of management financial documents that would allow financial analysis of the enterprise to be carried out quickly, qualitatively and affordable;



there is a steady tendency of increasing the number of enterprises engaged in international business;

the output of Azerbaijan enterprises to the international financial markets requires the provision of financial statements in accordance with international standards, as well as the transition to Western practice of accounting.

the need for significant foreign investment;

gradual integration into the European economic space. The main advantages in forming financial statements, there are no boundaries:

possibility to receive loans with a foreign bank;

the possibility of receiving foreign suppliers;

to function as a transnational company;

the possibility of obtaining a credit rating from a special agency;

possibility of attracting foreign clients;

availability of information and transparency of market participants;

the control over the financial status of the organizations and the activity of the organizations is improved;

the ability to compare companies with each other;

So, the benefits of compiling financial statements according to international standards are indeed and they are irrefutable for most users of financial statements. IFRS can be regarded as an instrument of globalization of the economy and world economic relations. Principles laid down in the order of reporting according to IFRS, make it adequate and capable of reflecting the true property of the organization. In connection with the connection value. IFRS is

important not only for foreign but also for national investors as well. This once again confirms the necessity and usefulness of the implementation process. IFRS for all sectors of the economy of Azerbaijan.

IFRS today is in a phase of continuous improvement. There is an opinion that the bankruptcy of corporations such as ENRON and World Com testifies that there is a need for significant transformations in IFRS and all this points to some problematic aspects during the transition

Azerbaijan to international standards, or rather too fast adaptation. But with this one should not agree, after all, the shadowing of the economy, high rates of taxes and deductions, the complexity of their calculation, considerable and the deterioration of fixed assets are the realities of the economy of Azerbaijan. Integration of Azerbaijan with member countries. The EU is not possible without internal economic activity, increasing the competitiveness of goods and after the introduction of the enterprise.

### **2.3 Fundamental assumptions and qualitative characteristics**

The International Accounting Standards Committee (IASB) described the underlying assumptions and qualitative characteristics of financial reporting, which are attributes that make the information presented useful to users. It should also be taken into account that additional information is imposed on information meeting the criteria of relevance and reliability. The relationship between the various characteristics of information and the constraints imposed is shown in the following diagram.

#### *Accrual basis*

Financial reporting in accordance with IFRS is prepared on an accrual basis. Accounting on an accrual basis is as follows: the results of transactions

and other events are recognized on the fact of their commission, and not when the funds are received or paid.

The application of this principle allows the interested user not only to analyze past transactions related to the payment and receipt of funds, but also informs users of financial statements of obligations to pay money in the future and about resources to be received in the future.

The opposite of the accrual principle (the principle of temporary certainty of facts of economic activity) is the cash method. Cash method involves accounting for income and expenses only at the time of receipt or payment of money.

Financial statements ought to be prepared on an accrual basis. This principle affects the financial statements as follows:

- it is required to recognize transactions and events at the time when they occur, and not when cash is paid or received;

- this entitles you to receive cash or other financial resources that were expressed in the balance sheet as assets;

- it obliges to pay cash or provide services, which were reflected in the balance sheet as liabilities;

- In the income statement it is required to reflect income and expenses in the terms to which they relate;

- the accrual principle is consistent with the principle of compliance, ie income is recognized at the time of sale of goods or services, regardless of the time of receipt of funds. When using the accrual principle, expenses are recognized in the period when the income associated with them is recognized, regardless of when the funds are paid.

The national Accounting and Reporting Standards (RAS), as well as in IFRS, establish the accrual principle. However, the implementation of this principle is not yet fully in accordance with IFRS, as Article of the Law of Accounting June 29, 2004 "On Accounting" established that accounting is conducted on the basis of primary accounting documents. Therefore, the costs related to this reporting period, without the presence of primary documents, can not be reflected in accounting as the costs of the reporting period, and this distorts the financial result of the activity. In accordance with IFRS, costs, even in the absence of primary documents, should be accrued and reflected in the reporting period to which they relate.

#### *Method of business continuity*

Annually a certain number of organizations cease to exist, but most companies continue rhythmic activity. Accounting assumes that the enterprise will exist and act in the future, this approach is called the principle of continuous activity. Since accounting is based on the principle of continuity, it does not contain information about how much the enterprise's funds could have been realized if it had ceased to operate.

From the principle of business continuity follows the cost method. According to this approach, accounting operates with the cost of funds, and not with their real market price.

#### *Qualitative characteristics of financial statements*

A reliable and objective presentation of the property and financial position of the organization can be performed only when applying the main qualitative characteristics of financial statements. The main qualitative characteristics are clarity, relevance, reliability and comparability.

\* a clearness is associated with the transfer of the meaning embedded in the transmitted information.

The main quality of information presented in the financial statements is its accessibility for understanding. The accountant prepares the report in accordance with the accepted practice, presenting the information in a manner understandable to the user. A financial statement user should be able to interpret this information and use it in making a decision, while he independently determines what information to use, how to use it, and what is the point of it. It is assumed that for this purpose users should have sufficient knowledge in the field of business and economic activity, accounting and the desire to study information with due diligence. However, information about complex issues that need to be reflected in financial statements because of their importance for economic decision-making by users is not to be excluded only because it may be too complicated to understand.

\* relevant information is information useful to users of financial statements, on the basis of which certain decisions are made.

Information is suitable when it affects the economic decisions of users, helping them estimate past, present and future case, confirm or correct their past valuation. Forecasting and confirming functions of information are connected in each other.

For instance, data about the present level and structure of existing assets is of cost to users when they try to predict the capacity of a company to take advantage of opportunities and respond appropriately to an unfavorable situation. The same data plays a supporting role in respect of past prognosis, for instance, concerning the possible structural organization of the company or the result of planned operations.

Information on the financial position and performance of past periods is often used to predict future financial position and performance, as well as other aspects directly interested in users. In order to have predictive value, the information should not have the form of an clear forecast. However, the ability to predict based on financial statements is enhanced by the manner in which information about transactions and events of past periods is presented.

The truth of information is affect by its nature and importance. Materiality is understood as the relative importance of a given object or event. The essentiality or importance of information is displayed in the event that its omission or erroneous calculation can affect the decisions made by users.

If an object or event is significant, then, most likely, for the user of the financial report, information about this will be appropriate. In other words, an object or event is significant if, in the absence of information about them, the user behaves differently than when this information was known.

Materiality depends on the size of the object, error, skip or distortion. Thus, materiality, rather, shows a threshold or a reference point and is not the main qualitative characteristic that information should possess in order to be useful.

The substance of an object is usually determined by relating its value to the value of a particular element of the financial statements, such as net income or total assets. Some accountants are of the opinion that if the accounting object is more than 5% of the total assets, then it should be considered significant. Materiality depends not only on the value of the object, but also on its nature. A large number of minor errors in the end can also lead to a significant magnitude. The essentiality of a particular accounting object or event is determined by the accountant preparing the report, and the user relies on the truthfulness and reliability of the information provided to him.

\* Accounting information must be reliable. In other words, information is reliable when users can rely on it as representing truthfully what it either has to represent, or it is reasonably expected from it that it will represent it. It must correspond to the purpose for which it was prepared, to be reliable and objective, that is, that independent parties could verify it using the same measurement methods.

To be reliable, information must provide a true picture of operations and other events. A true presentation assumes that there are no significant errors and deviations in the financial statements.

In order for the information to be trusty, it is very important that it be neutral, that is, impartial. Reporting should be objective and not designed for a specific user, which can in some way affect the decision-making. Financial reporting should not pursue the goal of inducing the user to a particular behavior.

Accountants try to build on facts and logic. This allows them to give the most reliable information about past events of the economic activity of the enterprise. Nevertheless, in the analysis and assessment, the accountant often faces uncertainties. In such cases, rely on the principle of prudence (conservatism). Diligence (conservatism) means caution in the formation of judgments that are necessary in calculations in conditions of uncertainty, i.e., the accountant should be more willing to recognize costs and liabilities than income and assets.

To be reliable, the information contained in the reports must be complete. The completeness of the information implies that the financial report and accompanying explanatory notes contain all relevant information necessary for users to understand this report. In other words, the reporting information should provide the necessary explanations and explanations in order to avoid the

possibility of misleading the user, and the format of financial reporting may affect its usefulness in making certain decisions. Elucidatory notes are considered an integral part of the financial statements. But , there is a limit after which there are so many explanatory remarks that they are more likely to mix than to help understanding. Consequently, company management and accountants, following the principle of completeness, decide what information should be disclosed beyond what is prescribed by the standards.

Recently, users of financial information themselves have influenced the understanding of the principle of completeness. To protect investors and creditors, auditors, stock exchanges and government agencies began to make more disclosure requirements. Therefore, the information provided by the company to the public is now more accessible and more comprehensive than before.

\* Users should be able to contrast the company's financial statements for different periods in order to define trends in its financial situation and performance. Users should also be able to compare financial reports of various companies operating both domestically and in other countries to assess their relative financial position, performance and changes in financial position. The information contained in the financial statements should be comparable in time and comparable with the information of other enterprises, that is, when the accounting methods (accounting policy) change, it is necessary to adjust the reporting data in accordance with the adopted changes (both in this reporting period and in previous accounting periods).

For this reason, the accounting methods used should be disclosed and used in a consistent manner. Users of financial statements should be informed of any changes in the methods, the consequences of these changes and should be able to determine the differences between the accounting policies. The principle of comparability, however, does not mean the same thing and the same method



must be followed all the time, even if this is to the detriment of the principles of relevance and reliability.

*Limitations on the appropriateness and reliability of information*

There are lots of restrictions that need to be charmed into account when presenting financial information in an appropriate and valid manner.

\* Timeliness is one of the limitations, as an unreasonable delay in the presentation of information can lead to the fact that financial statements lose their relevance.

In the event of undue delay, management may need to equilibrium the relative achievements of timeliness with the supply of trusty information. For the timely presentation of information, it is often necessary to report to the clarification of all aspects of an operation or other event, thereby reducing reliability. Conversely, if the reporting is decelerates until all aspects have been explained , the information can be extremely reliable, but not very useful for users who had to make decisions earlier. In reaching an equilibrium between relevance and reliability, the prevailing consideration is the best satisfaction of users' needs for economic decision-making.

\* The balance between benefits and costs is a general limitation in financial reporting. In spite of the fact that, in principle, the costs of presenting information to users should not exceed the benefit from receiving it, this is a subjective and often controversial issue. Naturally, for the information to be useful, it must have, at least, a minimum level of relevance and reliability. International and national organizations involved in the implementation of standards are working hard to determine what this minimum level should be. However, outside the provision of this minimum level, accountants and information companies in each case have to make decisions on what should be the ratio between benefits and costs. Most of the costs for obtaining information

are accounted by who prepared them , the benefit is acquired by both users and preparers. Ultimately, costs and benefits shift to society in the form of prices and public benefits from a more efficient allocation of resources.

\* The accountant in the preparation of financial statements should achieve an optimal balance between the qualitative characteristics of financial statements for a reliable image of the financial post of the enterprise.

In practice, it often requires an equilibrium or a compromise between qualitative characteristics. The relative significance of individual characteristics in different moments is professional judgment.

A professional judgment had to understand as a reasonable opinion of a professional accountant in respect of ways to qualify and disclose reliable information about the financial condition, financial results of the organization and their change.

### **CHAPTER III. INTERNATIONAL FINANCIAL REPORTING STANDARDS IN THE ACCOUNTING TRANSFORMATION SYSTEM**

### **3.1 Stages of progress of accounting and reporting in the medium term**

In our Republic, the transition to mandatory use of International Financial Reporting Standards is expected to be carried out in stages. Decree of the Government of the Azerbaijan Republic of June, 2006 No. i-38 approved the Program for Reforming Accounting in accordance with IFRS. As a goal of reforming the accounting system, the Azerbaijan accounting system has been brought into line with the requirements of the market economy and IFRS. The program provides for the development of a system of accounting and reporting standards that provide useful information to users; ensuring the linking of the accounting reform in Azerbaijan Republic with the main trends in the introduction of standards at the international level; providing methodological assistance to organizations in understanding and implementing a reformed accounting model.

It is supposed to improve the regulatory legal regulation, the formation of a regulatory framework (standards), methodical support (the publication of instructions, guidelines, comments ).

Order No. i-38 of the Minister of Finance of the Republic of Azerbaijan June 18, 2006 approved the "Concept for the Development of Accounting and Reporting in the Republic of Azerbaijan for the Medium-Term Perspective" aimed at improving the quality of information generated in accounting and reporting and ensuring guaranteed access to it by interested parties users.

Implementation of the Concept should be carried out according to special plans covering all the identified areas of development of accounting and reporting.

In the period 2006 - 2016 y. The following stages of the Concept implementation are envisaged.

2006-2010. Mandatory translation into IFRS of consolidated financial statements of socially significant economic entities (economic entities whose commercial activities involve directly or indirectly the funds of an unrestricted circle of persons: open joint-stock companies and other organizations that have publicly placed (placed) and (or) publicly traded securities; financial organizations that work with funds of individuals and legal entities, other organizations), except for those whose securities are traded in the stock markets of other countries and which constitute such statements by other internationally recognized standards. Approval of the main set of Azerbaijan standards for individual financial statements based on IFRS. Improving the principles and requirements for the organization of the accounting process, as well as the basic rules of accounting, providing information for the preparation of individual and consolidated financial statements. Creation of a special body within the system of approval (approval) of accounting and reporting standards. Creation of basic elements of the IFRS application framework. Approximation of the rules of tax accounting with the rules of accounting. Increasing the participation of professional public associations in the development and regulation of the accounting and auditing profession. Strengthening control over the provision of consolidated financial statements by publicly significant economic entities. Improvement of the system of training and professional development of personnel, including users of financial statements. Development of international cooperation in the field of accounting, reporting and auditing.

2010-2016. Mandatory translation into IFRS of consolidated financial statements of other economic entities, including publicly significant ones, whose securities are circulated in the stock markets of other countries and which compose such reports under other internationally recognized standards. Evaluation of the possibility of drawing up individual financial statements directly by IFRS (instead of Azerbaijan standards) by certain circle of economic entities. Strengthening and expansion of the scope of activities of the special

body within the system of approval (approval) of accounting and reporting standards. Further increase of the role of professional public associations in the development and regulation of the accounting and audit profession. Development of a system to control the provision of financial statements by business entities. Expansion of the scope of control for the quality of financial statements, including those prepared under IFRS.

### **3.2 Role of International Financial Reporting Standards in the Accounting Transformation System**

Accounting is an integral mechanism for managing a company in any country. Until the early 1970s, there were no unified methodological and technical methods of accounting, each state established its own rules. But business development has made its own adjustments. In the second half of the 20th century, the number of transnational corporations increased sharply, and there was a trend towards international integration in the economic sphere. The growth of business activity is impossible without the unification of accounting, since differences in accounting systems lead to certain difficulties:

- Investors find it more difficult to export their capital abroad, since differences in accounting systems lead to additional costs associated with the analysis of financial statements, for example, it is necessary to analyze the "quality" of profit;
- Accountants are more difficult to move to work in other states;
- programmers find it more difficult to create and implement software products.

Two approaches to solving the problem of unification of accounting have become widespread: harmonization and standardization, but at present these terms are often used as synonyms.

The idea of harmonization does not provide for a uniform for all countries model of accounting and uniform standards, it is believed that these standards should not contradict similar standards in other countries. The idea of harmonization is being realized within the European Community.

Standardization of accounting procedures is conducted by the Council for International Financial Reporting Standards - IASB. The IASB develops and publishes International Financial Reporting Standards. To ensure standardization of accounting procedures, it is necessary to develop a unified set of standards that could be applied in any country and thereby ensure a uniform approach to the formation of financial statements. This approach is an ideal form of standardization of the accounting process, but, as many economists and professional accountants believe, this should not be achieved by legislative means, but it is essential to perform mass outreach and involve professional organizations of different countries for this.

Accounting is an indispensable tool for the implementation of various property relations, both private law - between business entities, and public-legal, tax relations - with the state.

### **3.3 International and national Financial Reporting Standards**

The need for a fundamental change in the existing norms and rules of accounting in connection with the change in the system of public relations and the civil law environment was reflected in the accounting reform. The purpose

of reforming the accounting system is to bring the national accounting system in line with the requirements of the market economy and IFRS.

*Reform tasks:*

- Forming a system of accounting and reporting standards that provide useful information to users, primarily investors;
- ensuring the linking of the accounting reform in Azerbaijan with the main trends in the harmonization of standards at the international level;
- providing methodological assistance to organizations in understanding and implementing a reformed accounting model.

The globalization of the capital market requires comparability of the information provided, in connection with which the national system of accounting standards will be developed on the basis of IFRS. The purposes of development of accounting:

- creation of an accounting system that is compatible with IFRS;
- ensuring practical application of IFRS as the only accounting standards for the preparation of financial statements by securities issuers;
- development of the accounting profession.

The reform of the accounting system in Russia is aimed at ensuring transparency, clarity and reliability of financial reporting of companies to qualified users.

Currently, many Azerbaijan organizations are experiencing a significant shortage of current assets, which significantly impedes the economic growth rates not only of these companies, but also of Azerbaijan as a whole. To overcome this situation, investments are required, including investments by

Western partners. However, investing significant amounts of cash, investors require companies to provide understandable accounts. This means that reporting should not only be translated into a foreign language, but also compiled in compliance with certain rules. The basic rules of accounting and reporting that are clear to all qualified Western users are IFRS.

Many believe that the transition from this situation may be the transformation of financial statements, but the transformation of financial statements in accordance with IFRS is only the first (mandatory) step in the way of transition of Azerbaijan enterprises to international financial reporting standards. This is because of the fact that large enterprises in the case of not Russia's transition to IFRS will incur double costs for the preparation of financial statements. First, they will be required to report in the format of Azerbaijan financial reporting standards and conduct an audit. Secondly, companies will need to generate IFRS statements and receive an audit opinion on it.

The need to reform the accounting system is beyond doubt. For successful implementation of this reform, it is necessary to allow all large companies whose shares are traded on international stock markets to compile all financial statements only in accordance with the requirements of IFRS and to save them from high expenses for the transformation of financial statements or the maintenance of parallel accounting.

Currently, there are several organizations in Azerbaijan implementing projects on accounting reform. Among them, for example, the Ministry of Finance. At the end of 2017, MF completed the development of recommendations for the implementation of IFRS. The main provisions of the recommendations are as follows:



- Immediate transition to IFRS for banks and organizations whose shares are listed on the stock exchange;
- when selling significant amounts of state-owned blocks of shares, the financial statement under IFRS should be included in the information prospectus;
- unitary enterprises undergoing compulsory audit should prepare financial statements in combination with IFRS;
- Azerbaijan accounting standards should be aimed at meeting the needs of small businesses and companies with a limited number of participants;
- it is necessary to ensure the preparation and dissemination of methodological recommendations, explanations and examples of practical use of IFRS at Azerbaijan enterprises, and so on.

*Differences in the maintenance of accounting under international financial reporting standards and Azerbaijan accounting rules*

For decades, the development of accounting theory in Azerbaijan has been divorced from world experience. Recently there has been a gradual adaptation of the system of Azerbaijan accounting to the requirements of a market economy and the gradual approximation of NAS to the requirements of IFRS. In this regard, developed and used:

1. New Azerbaijan Accounting Standards:
2. New forms of financial reporting, method of accruals.
3. Different definition of expenses for tax purposes and preparation of financial reporting documents.
4. Reserve funds and valuation reserves.

## 5. Consolidated financial statements.

Differences between international financial reporting standards and the Azerbaijan accounting system can be explained by various factors, such as users of financial statements, historical factors of economic systems development, the role of professional associations of accountants and auditors in the development and adoption of accounting standards and rules, and in their practical application.

Although there are certain world trends, each country in its economic, political, social and cultural development is individual. All countries use the accumulated world experience to achieve internal goals set for the development of the economy. Including the development of basic accounting procedures. Almost every country develops its own regulatory documents (standards) for accounting and reporting. Normative acts of each country have both common features (principles and qualitative characteristics) and differences (the purpose of reporting, the regulation of accounting and reporting rules, the connection of financial statements with tax legislation, the frequency of reporting).

When analyzing the requirements and approaches of IFRS and NAS, it is also possible to distinguish differences in the composition and content of reporting forms.

In accordance with the Azerbaijan statutory acts on accounting, the full set of annual financial statements includes:

1. The balance sheet.
2. Profit and Loss Statement.
3. Appendices to the financial statements:
  - o Statement of cash flows.
  - o Statement of changes in equity.

- o Appendix to the balance sheet.
- o Report on the intended use of the funds received.

4. The audit report.

5. Explanatory note.

In accordance with IFRS, the set of annual financial statements includes:

1. The balance sheet.

2. Profit and Loss Statement.

3. Statement of changes in equity.

4. Statement of cash flows.

5. Accounting policies and notes to the financial statements:

- Statement of compliance with International Financial Reporting Standards.

- Information on the applied basis (s) of the valuation and accounting policy.

- Supporting information for the articles presented in each form of financial statements in the order in which each line item and each form of financial reporting is presented.

- Other disclosures, including: contingent events, contractual obligations and other financial disclosures and disclosures of a non-financial nature.

These differences cause the need to move in the accounting reporting from Azerbaijan standards to international ones, this transition should be considered as a separate task, which is solved on demand of circumstances of entrepreneurial activity.

## CONCLUSION

The process of unification of accounting systems in different countries is to ensure transparency of reporting and reflection of the real economic situation in the company, which will allow users of accounting to make the right economic decisions. However, any changes in the accounting system are costly and time-consuming, and the comparable economic benefits of such a unification should be evident. The introduction of IFRS in a particular country will cause an adjustment of national accounting rules and regulations. Although this will require significant efforts and means, improving the quality of the reporting information will result in resource savings, eliminating the double burden on companies that are now compelled to report in the system of national standards and IFRS, will facilitate the adoption of more effective management decisions.

At the current stage of development and harmonization of accounting and reporting, the International Financial Reporting Standards are applied in the following cases:

- application of IFRS by individual economic entities on a voluntary basis;
- as a criterion for admission to capital markets;
- Use along with national standards;
- adaptation of national standards to IFRS;
- application of IFRS as national standards.

Recently, for most countries in the world, the problem of international unification of accounting is becoming increasingly important. The active development of business is accompanied by the strengthening of the role of international integration in the sphere of the economy, which imposes certain requirements on the uniformity and understandability of the principles of

formation and algorithms of calculating profits, the taxable base, the terms of investment and capitalization of earned funds, etc., used in different countries.

Currently, international standards are mainly used by large Azerbaijan companies, oil and gas enterprises and banks, for example, Socar, NB of Azerbaijan and other. The application of IFRS will develop as Azerbaijan companies realize the benefits of using international standards: optimizing the decision-making process, increasing the confidence of counterparties and creditors, and so on.

In Azerbaijan, one of the most rational ways of applying IFRS is their adaptation. It involves the gradual improvement of Azerbaijan accounting and reporting rules aimed at the formation of high-quality financial information in accordance with the requirements of international standards. This way of implementing IFRS corresponds to the approach of most European countries, therefore, brings closer economic integration, harmonization of accounting and reporting systems. It is especially important that, as a result of the adaptation, the comparability of the financial statements of Azerbaijan and foreign companies is achieved.

When writing the work, sources were used that dealt with the problem of Russia's transition to IFRS. Particular attention was paid to the regulatory framework of accounting in Russia. Some of the information was obtained on the official website of the IASB in the worldwide electronic network.

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