

University of Economics in Prague

Faculty of Finance and Accounting

Finance and Accounting



MASTER THESIS

Auditor independence and professional
ethics

Author: Bc. Gafurova Nasiba

Supervisor: doc. Ing. Vladimír Králíček, CSc.

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Declaration of Authorship

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Abstract

The purpose of the submitted thesis "Auditor independence and professional ethics" is to review and analyse the role of independence and ethics in audit profession. The first part is devoted to the role of the audit and auditing in global world. The second part focuses on the audit in Uzbekistan. The third part is dedicated to the role of ethics and independence in audit profession. The pre-last part is about new approach to the Code of Ethics and the main changes in the new regulatory document. And the last part consists of comparative analysis of the new and previous legal documents.

JEL Classification

M40, M42, M48

Keywords

Accounting, Auditing, Audit, Audit Firm, Auditor, Auditor Independence, Accounting Law, Accounting Standards, Auditing Standards, Financial Reporting Standards, International Accounting Standards

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Introduction

Economic success usually depends on the confidence of capital users and capital providers. The creditor would not lend to the borrower without enough information to convince the lender that the capital will be returned. Interest is established, subconsciously or in discussion, based on the creditor's view of the risk that the capital will not be returned. Subconsciously or in discussion, the sides establish the interest according to creditor's view of the risk that the borrower will not return the capital.

Auditors decrease financial expenses, help to efficiently allocate the capital. They build a basis for trust and confidence, contributing to economic growth. Due to skilled, professional and independent auditors investors are able to differentiate the real managers and frauds.

Representing the public interest in reliable information, the auditor gives popularity to management and takes the risk. The free market becomes possible by this moral choice. At the same time, the auditor also changes the behavior of the management of the audited organization. In this situation, the independent auditor is like an advocate of free markets.

As it was said by the Scotsman and father of modern economics, Adam Smith, the managers of the companies arrange other people's money and not their own money, "it cannot well be expected, that they should watch over it with the same anxious vigilance with which the partners in a private [firm] frequently watch over their own ".¹

Thus, the inspiration for the audit profession, created in the century after he wrote, to enable industrialists to amass the funds necessary for the great, capital intensive ventures of the 19th and early 20th centuries².

According to the idea of rationalist, the reason should encourage capital users to further develop our markets, supporting initiatives to expand the scope and independent verification and analysis of information.

The rationalist says that reason should motivate the users of capital to further develop markets by supporting initiatives to enhance the scope, and independent validation and information analysis. However, "*Treatise on Human Nature*" of Hume says that we are induced by a common, continually existing wish for pleasure and not by reason, but by a general, continually present desire for pleasure and the avoidance of hurt.

¹ *List of Cognitive Biases* | *The World Class R&D Institute*, www.worldclassrd.org/quotations/1168

² See The Joint Stock Companies Act of 1844 and the Companies Clauses Consolidation Act of 1845.

1. Audit profession in global world

1.1 Audit and auditing

Nowadays audit is required in almost every business organization, public and private company. Some companies do audit controlling as mandatory, but some of them ask auditors to make an audit control for their own benefits.

The audit is one of the fastest growing areas of the accounting sciences which is developing rapidly.

Being originated from Latin, the word "Audit" - audio, audire can be translated as "Listening". This word has had various classifications and definitions during the time. But in general it is a synonym to check, control, revise, inspect etc.

While accounting has changed in many ways over time, the audit has evolved continuously, responding to changes in the environment and changing its goals, beginning with middle age, going through the industrial revolution until the 21st century.

Companies prepare financial reports on their activities, which reflect their overall effectiveness. These financial statements are reviewed and evaluated by independent individuals who evaluate them in accordance with generally accepted industry standards. This examination and evaluation are called audits.

Before going deeply into the audit profession we need to know and understand what actually audit means and how different people define it.

Below we can find different examples of this definition:

- "Audit is the examination or inspection of various books of accounts by an auditor followed by physical checking of inventory to make sure that all departments are following documented system of recording transactions. It is done to ascertain the accuracy of financial statements provided by the organisation."³
- "An audit is an examination and verification of a company's financial and accounting records and supporting documents by an independent professional against established criteria."⁴

³ <https://economictimes.indiatimes.com/definition/audit>

⁴ "Audit Definition Objectives, Features, Origin (Explained)." *IEduNote.com*, 28 Aug. 2018, iedunote.com/audit

According to the International Federation of Accountants:

- "An audit is the independent examination of financial information of an entity, whether profit oriented or not and irrespective of its size, or legal form, when such an examination is conducted with a view to expressing an opinion thereon".⁵

According to Spicer and Pegler, an audit is:

- "Such an examination of the books, accounts and vouchers of a business, as will enable the auditor to satisfy himself that the Balance Sheet is properly drawn up, so as to give a true and fair view of the state of the affairs of the business, and whether the Profit and Loss Account gives a true and fair view of the profit or loss for the financial period, according to the best of his information and the explanations given to him and as shown by the books; and if not, in what respect he is not satisfied".⁶
- "Auditing is a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users (Boynton & Johnson, 2006)".⁷

It can be considered from the above definitions that the auditing is the systematic and professional examination of the accountant books and business records, and also enables the auditor to form an opinion that everything in the Balance Sheet and the Profit and Loss Account are properly recorded so it shows a correct and fair view of the financial condition of business affairs and profit or loss for the given financial period.

The auditor needs to go through different books and accounts and connected evidence in order to make sure about the accuracy and authenticity to report the good financial condition of the business. Results are quite important to the company's reputation and further success, that is why companies are expected to have their audits made.

Audits are very important for external company affiliates, like shareholders, stakeholders and other investors, as they provide an additional reassurance of their selection in investments in case if problems arise.

⁵ "Audit Definition Objectives, Features, Origin (Explained)." *IEduNote.com*, 28 Aug. 2018, iedunote.com/audit.

⁶ <https://practicalandprinciplesofauditing.wordpress.com/introduction-of-auditing/>

⁷ "Auditing Reflection Research Paper - 1200 Words." *StudyMode - Premium and Free Essays, Term Papers & Book Notes*, www.studymode.com/essays/Auditing-Reflection-1873191.html.

1.2 Origin of audit and it's evaluation

Auditing of the accounts of public institutions was practised from the time of ancient Greeks, Romans and Egyptians. During that time checking clerks were supposed to control the public accounts. The main purposes of the auditing were to recognize frauds, to identify if the payments and the receipts are correctly recorded by the responsible people.

Only in the period of the industrial revolution, from 1750 to 1850, auditing began its evolution in the field of fraud detection and financial reporting.

During this time, the business developed and led to large-scale production, steam power, improved facilities and better cooperation and communications as well. This led to the emergence of joint-stock organizations.

Shareholders added their capital to those companies, but they did not control daily performance of the organizations. Shareholders who invested their money were interested in being aware of the situation, the financial position of the organization, however they hired management to operate businesses when the owners were absent.

They needed people who could work and observe financial activities, in order to prevent fraud and for accuracy. That is why investors wanted to hire an independent person, so he or she could check the accounts of the company, and afterwards report the investors on the accuracy of them and safety of their contribution.

In the beginning of the 20th century, the practice of auditor reporting, which included reporting on their responsibilities and results, was standardized as an "Independent Auditor's Report".

The development of the testing process was caused by increasing demand for auditors.

Auditors have developed a way to select key cases strategically as a representative of the overall performance of the company. This was an affordable alternative for detailed study of each case, and this took less time compared to a standard audit.

1.3 Objectives of the audit

Developing and improving from year to year auditing nowadays has its features, scope, objectives and so on.

The objectives of the audit can be divided into two parts, such as primary objectives and subsidiary objectives.

The primary objectives of the audit include:

- Inspecting of the internal check system;
- Checking and verifying the accuracy of accounts books, making sure about their fairness;
- Learning and making decision if the prescribed laws were followed while preparing the statements;
- Confirming the authenticity of transaction and their validations;
- Checking if the capital has proper distinction;
- Checking the revenue from transactions;
- Giving confirmation regarding the existence and value of assets and liabilities;
- Giving an independent opinion as a conclusion.

The subsidiary objectives of the audit consist of :

- Detection of errors;
- Prevention of errors;
- Detection of frauds;
- Prevention of frauds.

Because of some limitations of financial statements it is difficult to provide a hundred percent accuracy, that is why auditors try to show the fair view of those records. The financial records can show accurate, fair and true view after auditing processes. So determination of the fairness of the statements is the purpose of the auditing.

There are different laws which regulate the working processes of the businesses. The auditors should give an opinion after checking, whether the prescribed laws were

followed while the final statements were prepared. Checking if the appropriate laws were followed is the purpose of auditing.

In order to prepare accounting records, accounting policies should be followed. Results are much better when accounting system is effective. After examining the accounting policies, the auditor can give an opinion on them in the best interest of the audited business. So we can say that examining the accounting policy of the organization is another purpose of the auditing.

The auditor should be honest in his work and express an independent opinion on what he has examined. The other people and management of the companies should not influence on auditor. High ethical standards should be followed for independent reporting.

Because of large amount of work or lack of attention mistake can occur in the financial statement. Employees should not be burdened with extra work and senior person should control the work of junior one.

Another purpose of the auditing is to recognize and correct the mistakes. And the auditor can use different means and ways to identify the errors in the accounting books. It is very useful to have an internal check in order to prevent frauds. The audit should recognize the frauds in financial records and prevent further ones. Various types of frauds can be detected in the statements and some examples are alteration and manipulation of records, asset's misappropriation, misapplication of accounting policies, transaction which are recorded without substance and so on.

1.4 Quality of an auditor

It is well-known that people of different professions must have some appropriate qualities. Being appointed to care about the interests of investors and the owners of the business, the auditor protect their property. Auditor must let the owner know when he sees that their rights are affected by wrong actions of the management. In order to protect the rights of the owners, auditor must do his best for detecting frauds and errors in the financial statements.

The auditor can not demonstrate his favour towards people who is responsible for manipulation and negligence of financial statements. If the management has been found guilty of making errors and frauds, the auditor should not protect them in those matters. In case if the management is not able to protect the rights of investors, the auditor can report it to them.

As a professional accountant, an auditor has the duty to reasonable care and skill conducting the audit. Before starting his audit work, he must check the organization's internal control system. An auditor is obliged to verify the assets and liabilities personally. He must control if the accounting records were made according to generally accepted accounting principles. If an auditor has any doubt concerning the errors and fraud, in order to clear it, he has to investigate the matter in depth.

In order to work as an auditor, the person should have some professional and personal qualities. Professional qualities may include accounting knowledge, auditing, taxation laws, company law, business organization and operation, preparation of budget, electronic data processing and general knowledge.

1.5 Professional qualities

- a) Accounting. The accounting system contains procedures, various records, personnel, forms and other devices which are used by any business. Accounting is a process that continuous for the whole yearly period. Being an expert in accounting field, an auditor knows its methods, principles and techniques.
- b) Auditing. As an expert in accounting field, an auditor knows the regulations and rules concerning the audit. The auditor is an experienced person in the field of auditing, and he knows how to check accounting records and any other financial performance.
- c) Taxation laws. It is very important for the auditor to have knowledge of taxation. He must know different acts regarding the taxes and tax rates.

- d) Company law. Dependent on the company where the auditor is making an audit control, he should know internal rules of the organization.
- e) Business organization and operation. The auditor must be informed about the organization structure of the company and its business. The placement of the workers on the job is known as an organizational structure. The auditor has to know the working of different departments of the business.
- f) Preparation of the budget. While preparing the budget, the figures are taken from the last year and estimations are made for the next year. The auditor must be an expert in this case. Besides it, all functions, i.e departments of the business concern requires various budgets.
- g) Electronic data processing. In global world the computers are used in business for accounting and other financial purposes. The auditor should be trained to process the data through computers.
- h) General knowledge. The auditor has to have knowledge of common science. He should have some ideas about the financial, economic and political conditions. The auditor should have the latest knowledge which effects the business concern.

Moreover, the auditor should have personal qualities, such as tact, honesty, independence, vigilance and leadership.

- a) Tact. In order to give comments and criticize policies of the management, the auditor should have technical information. In case of missing information, he will be able to collect it with argument and discuss without offending them.
- b) Honesty. The auditor must be honest in his professional work and act straightforwardly. He should realize that reporting true and fair view of business matters is his duty. The auditor has to have really high moral standards.

- c) Independence. During the time of investigation, programming and reporting the auditor must be independent. Management and other people should not influence him neither directly nor indirectly.
- d) Vigilance. The auditor knows much about activities of accountants and audit staff. He is able to identify errors and frauds due to vigilance. He is open-eyed in watching the audit work.
- e) Leadership. As an auditor is a leader of an audit team, he can guide the auditors by demonstrating on himself how to work. The senior and junior audit clerks usually work under his leadership.

1.6 Auditors and audit firms

The market of audit services is kind of oligopoly. All of the accounting firms can be divided into 3 groups:

1) The first tier accounting firms:

- Deloitte Touche Tohmatsu Limited;
- PricewaterhouseCoopers (PwC);
- Ernst & Young (EY);
- Klynveld Peat Marwick Goerdeler (KPMG).

They are also known as a "Big four". The Big four is the 4 largest accounting firms in the world. They provide wide range of accounting and audit services to their clients. The services include external audit, management and business consultancy, taxation services, corporate finance and legal services, risk assessment and control.

Those firms provide massive employment and career growth opportunities to auditors and accountants around the globe.

2) The biggest second tier accounting firms⁸:

- BDO;
- RSM;
- Grant Thornton;
- Crowe Horwath;
- Baker Tilly;
- Nexia International.

The second tier firms are much smaller than the first tier firms. The highest revenue of the firm from second tier is only 8 mln \$ per year. They offer the same kind of services like a Big four firms, but in a smaller globe scale and all have less than 100 000 employees.

⁸ <https://big4accountingfirms.com/2nd-tier-accounting-firms-list/>

Statistical data about the second tier firms:

Company name	Revenue in bln USD, 2017	Number of employees ⁹ , 2017	Services
BDO	8.1	74 000	-Audit and assurance -Advisory -Tax
RSM	5.1	43 000	-Audit and assurance -Tax -Consulting -Risk advisory -Specialist services -Outsourcing -Restructuring -Transaction advisory
Grant Thornton	5	50 000	-Advisory -Audit -Tax -Integrated services
Crowe Horwath	3.8	36 000	-Audit -Tax -Advisory -Risk consulting -Performance consulting
Nexia International	3.62	30 000	-Audit -Tax -Advisory
Baker Tilly	3.4	33 000	-Audit and assurance -Tax - Speciality advisory services

Table 1. Second tier firms: their revenue, number of employees and services.

⁹ Around this amount

- 3) Local firms. Local firms can be big as well, but usually they operate only in the given region.

1.6.1 The Big four accounting firms

The Big four or the first tier accounting firms basically run the accounting industry. Their services are not limited with public companies. They also provide their services to private companies, non-profit organizations and high wealth individuals.

Due to their dedication to integrity these accounting firms have gained trust and respect of the society. Their performance is associated with quality and professionalism and highly respected. In other words, the Big four firms symbolize ideals of the public accounting profession and industry at all.

Actually, those companies are not 4 individual companies. They are four large networks of member firms, often called a professional services network. They are located around the world.

With a membership agreement in place to share the company name, brand, image and standards, each network is owned and operated independently from one another.

1.6.2 Deloitte Touche Tohmatsu Limited

Deloitte Touche Tohmatsu, known among people as just "Deloitte", was established in 1845, by William Deloitte. The company has seen a series of managers and reorganizations. In spite of this fact, Deloitte could keep its brand name with its quality standards and company values as well. Nowadays it operates as one of the most successful brands in the globe.

In 2017, the revenue was equal to \$38.8 billion and had around 263,900 employees in more than 150 countries showing excellence in providing audit, financial advisory, consulting, risk management, and tax services to clients around the world. Deloitte is the largest company among the Big four.

1.6.3 PricewaterhouseCoopers (PwC)

The company was established in 1998 by the merger of two large accounting firms – Price Waterhouse and Coopers & Lybrand. Organizations decided to join and were dedicated in providing services of value. They established and maintained good customer relations at the same time.

PwC firms operate locally in different countries around the world. These firms are owned and managed independently and share common values and standards, as other international companies. PwC provides excellent assurance, consulting, tax and other services.

PricewaterhouseCoopers is the second largest accounting firm in terms of revenue. In 2017, it earned \$37.7 billion. The company employs more than 236,200 professionals in over 150 countries around the world.¹⁰

1.6.4 Ernst & Young (EY)

Ernst & Whinney joined with Arthur Young to found Ernst & Young in 1989. Ernst & Young is a global organization of member firms. It operates in more than 150 countries. The company employs people with professional skills and values of cooperation, teamwork, respect, motivation and enthusiasm. These form the core values of Ernst & Young.

Ernst & Young also appreciates knowledge and skills development. It helps around 247,570 employees reach their potential by providing professional training and career development programs. The organization offers assurance, tax, advisory, and special services. Ernst & Young had a revenue equal to \$31.4 billion in 2017.¹¹

1.6.5 Klynveld Peat Marwick Goerdeler (KPMG)

Klynveld Peat Marwick Goerdeler popularly known as just KPMG is a network of accounting firms operating globally. They provide audit, assurance, advisory, tax and

¹⁰ <https://www.accountingverse.com/articles/big-4-accounting-firms.html>

¹¹ “Big 4 Accounting Firms - Who They Are, Facts and Information.” *Accountingverse.com*, www.accountingverse.com/articles/big-4-accounting-firms.html.

legal, and enterprise services. The company employs around 197,260 professionals cooperating with each other to provide high quality service in 154 countries around the world. KPMG earned \$26.4 billion in 2017.

The company was created in 1987 by merging of Peat Marwick International and Klynveld Main Goerdeler (KMG). Like any other organization, that provides professional services, KMPG places huge value on its employees and quality of service.

1.6.6 The history of Big four

The Big 4 was known as Big 8 and consisted of :

1. Arthur Andersen
2. Arthur Young & Co.
3. Coopers & Lybrand
4. Ernst & Whinney
5. Deloitte, Haskins & Sells
6. KPMG
7. Touche Ross
8. Price Waterhouse.

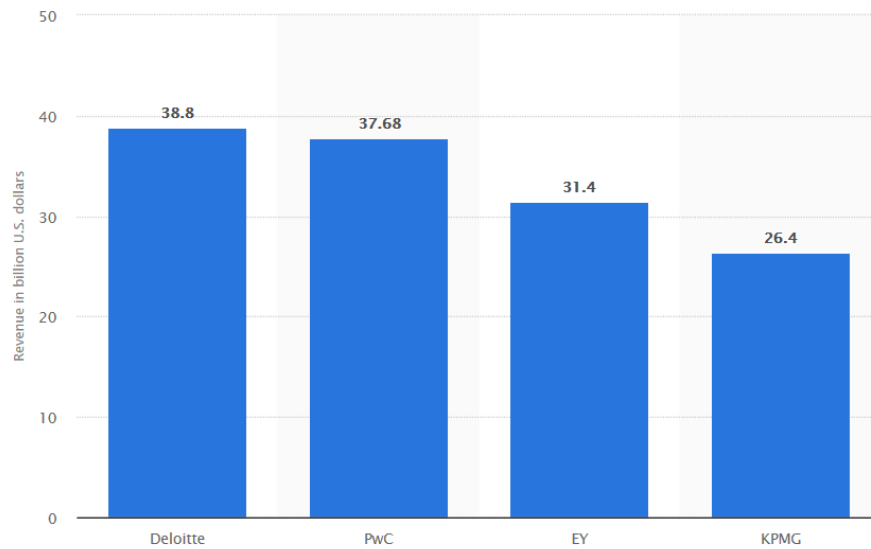
In 1989 due to the mergers of Ernst & Whinney with Arthur Young to form Ernst & Young, Deloitte, Haskins & Sells with Touche Ross to form Deloitte Touche The Big 8 became Big 6.

Then in 1998, Price Waterhouse merged with Coopers & Lybrand to establish new PricewaterhouseCoopers, popularly known as PwC. The Big 6 reduced to Big 5. In 2002, Arthur Andersen was involved in the world-shocking Enron scandal and fall of the group. Big 5 turned into Big 4. From that time on, the four biggest existing accounting firms were known as the Big 4.

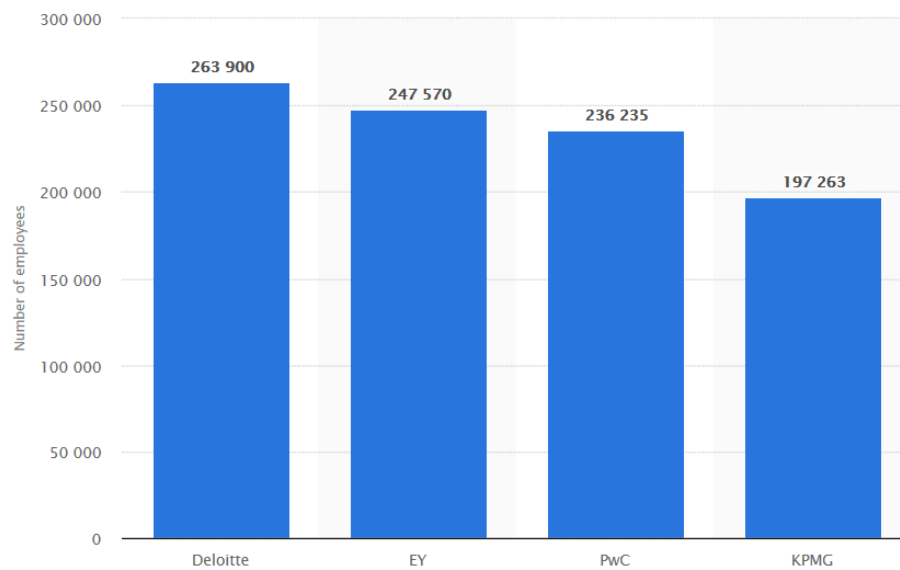
Statistical data about the Big four:

Company name	Revenue in bln USD, 2017	Number of employees, 2017	Services
Deloitte	38.8	263 900	-Audit and assurance -Risk advisory -Financial advisory -Tax -Consulting -Legal
PwC	37.68	247 570	-Audit and assurance -Advisory -Entrepreneurial and private clients -Family business -IFRS -Legal -People and organization -Tax -Sustainability and climate change
EY	31.4	236 235	-Advisory -Assurance -Tax -Transactions
KPMG	26.4	197 263	-Audit and assurance -Tax and legal -Advisory -Enterprise

Table 2. Big four accounting firms: their revenue, number of employees and services.



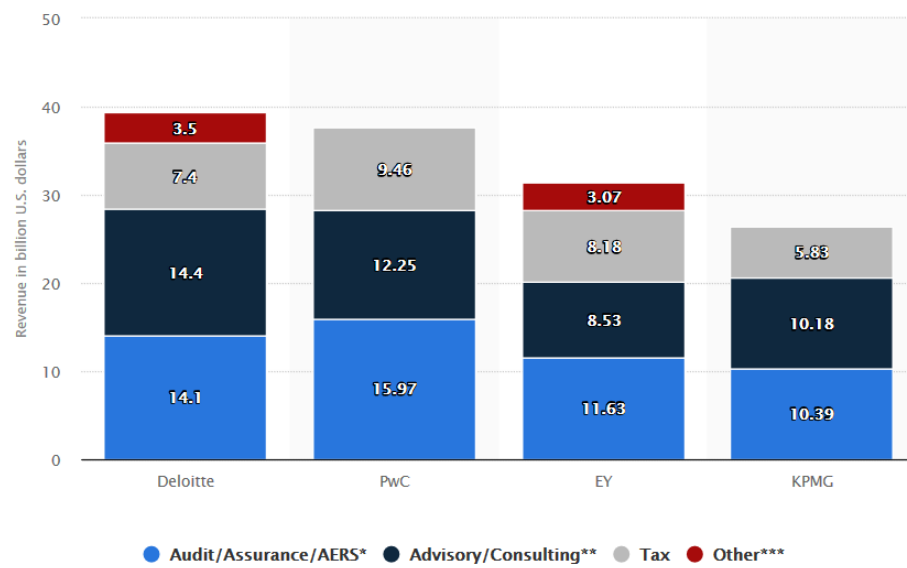
Graph 1. Revenue of the Big Four accounting / audit firms worldwide in 2017 (in a billion U.S. dollars)¹²



Graph 2. Number of employees of the Big Four accounting / audit firms worldwide in 2017¹³

¹² <https://www.statista.com/statistics/250479/big-four-accounting-firms-global-revenue/>

¹³ <https://www.statista.com/statistics/250503/big-four-accounting-firms-number-of-employees/>



Graph 3. Revenue of the Big Four accounting / audit firms worldwide in 2017, by function (in a billion U. S. dollars)¹⁴

¹⁴ <https://www.statista.com/statistics/250935/big-four-accounting-firms-breakdown-of-revenues/>

2. Audit in Uzbekistan

2.1 Information about the Republic of Uzbekistan

The Republic of Uzbekistan is a sovereign democratic republic in Central Asia. It is a unitary constitutional republic, which comprises 12 provinces and one autonomous republic- Karakalpakstan, and a capital city-Tashkent. It shares borders with 5 countries: Kazakhstan, Kirgizstan, Tajikistan, Turkmenistan and Afghanistan.

The common area of Uzbekistan is 447,8 thousand km² with population of 32.1 million people as of January 2017¹⁵.

Uzbekistan has got its independence from Soviet Union in 1991. Shavkat Mirziyayev is the President of Uzbekistan. The national language is Uzbek. The currency is som.

The economy of Uzbekistan is in a gradual transition to the market economy. It has foreign trade policy based on import substitution. In September 2017, the country's currency became fully convertible in the market rates. Uzbekistan is a main producer and exporter of cotton in the world. The country also operates the largest open-pit gold mine in the world. Uzbekistan has a gigantic power-generation facilities of the Soviet era and sufficient supply of natural gas. Uzbekistan is the largest electricity producer in Central Asia¹⁶. Renewable energy makes up more than 23% of the country's energy sector. Hydroelectricity has 21.4% and solar energy 2% respectively.

China National Petroleum Corporation, Petronas, the Korea National Oil Corporation, Gazprom, Lukoil, and Uzbekneftegas are the largest corporations involved in Uzbekistan's energy sector.

27% of Uzbekistan's labour force is employed in agriculture and they contributes significant amount of GDP. In April, 2018 the nominal GDP of Uzbekistan was equal to 40.259 billion USD.

According to a survey by global bank HSBC, Uzbekistan is predicted to be one of the fastest-growing economies in the world (top26).¹⁷

¹⁵ <https://stat.uz/uz/432-analiticheskie-materialy-uz/2033-o-zbekiston-respublikasining-demografik-holati>

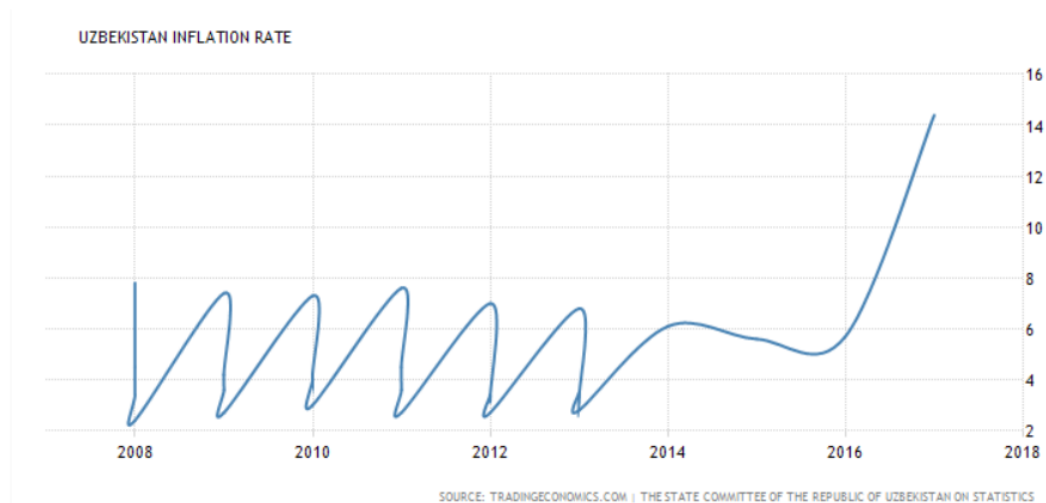
¹⁶ "Uzbekistan | Energy 2018 – Global Legal Insights". *GLI – Global Legal Insights Uzbekistan | Energy 2018*. Archived from the original on 3 December 2017. Retrieved 2 December 2017

¹⁷ "the World in 2050" (PDF). HSBC. p. 2. Archived (PDF) from the original on 14 October 2017.

GDP and inflation rate in Uzbekistan:



Graph 4. GDP of Uzbekistan (2008-2018)¹⁸



Graph 5. Inflation rate in Uzbekistan (2008-2018)¹⁹

¹⁸ <https://tradingeconomics.com/uzbekistan/gdp>

¹⁹ <https://tradingeconomics.com/uzbekistan/inflation-cpi>

The structure of the population in Uzbekistan:

	1991		2011		2017	
	number	share, %	number	share, %	number	share, %
Total	20607,7	100,0	29123,4	100,0	32120,5	100,0
uzbeks	14995,3	72,8	23983,2	82,3	26917,7	83,8
karakalpaks	431,9	2,1	641,5	2,2	708,8	2,2
tadjiks	980,7	4,8	1411,6	4,8	1544,7	4,8
kazakhs	845,3	4,1	832,7	2,9	803,4	2,5
russians	1593,8	7,7	837,5	2,9	750,0	2,3
kirgizs	182,6	0,9	254,6	0,9	274,4	0,9
tatars	414,6	2,0	218,6	0,8	195,0	0,6
turkmens	126,6	0,6	174,7	0,6	192,0	0,6
koreans	183,7	0,9	188,0	0,6	176,9	0,6
ukraineans	146,8	0,7	78,2	0,3	70,7	0,2
others	706,4	3,4	502,8	1,7	486,9	1,5

Table 3. The percentage of nations who lives in the territory of Uzbekistan²⁰:
(as of the beginning of 2017, in thousands)

2.2 Statutory Framework for Accounting and Auditing, overview

Accounting, auditing, and financial reporting requirements in Uzbekistan are stipulated in the Law on Accounting No. 279-I of 1996, as amended in 2016, and the Law on Auditing Activity No. 734-XII of 1992 as amended in 2000.²¹

Basic accounting and bookkeeping requirements are set up by the Law on Accounting for all organizations in the Republic of Uzbekistan. This law gives the right to the Ministry of Finance of the Republic of Uzbekistan to establish accounting standards for

²⁰ <https://stat.uz/uz/432-analiticheskie-materialy-uz/2033-o-zbekiston-respublikasining-demografik-holati>

²¹ “Uzbekistan.” *IFAC*, www.ifac.org/about-ifac/membership/country/uzbekistan.

the private businesses and for the organizations, financed by state. The Law on the Accounting does not regulate the audit in the banks and credit institutions.

International accounting standards such as IFRS and IAS were modified by the Ministry of Finance and adopted National Accounting Standards were represented. There is no exact timeline, but the full adoption of IFRS is under consideration.

Accounting requirements for banks and credit institutions are established by The Central Bank of Uzbekistan (CBU). In 2004 IFRS were adopted by CBU as existed for application in the financial statements of organizations under its control.

The accounting standards were not modified to incorporate subsequent changes to International Financial Reporting Standards.

Defining the requirements for audit of accounting records of all companies, The Law on Auditing Activity authorizes the CBU to set up audit requirements for banks and credit institutions.

Regarding to the Law, the following organizations should have the audit of their financial statements:

- Banks and other institutions which has the licence of CBU;
- All join stock companies;
- Insurance companies;
- Non-government organizations;
- Bourses²²;
- Charities;
- Investment and other funds, that administrates monetary investments of the public at large;
- Organizations where sole or one of the investors is a public sector organization.

Besides it, any other company can have the audit of their financial records based on their needs.

According to the Law on Auditing, the Ministry of Finance has the right to establish and enforce the standards of auditing. The Ministry issued the Uzbek National Standards of Auditing, and they are based on International Standards on Auditing (ISA) in effect as

²² The shares of some join stock companies are traded in "Toshkent" bourse. The "Toshkent" bourse was established on April 8, 1994 and has more than 100 broker offices.

per year 2008. At the same time, the Ministry of Finance stated that the goal is to fully approve the ISA and indicated 2017 as the year of expectation of adoption for all official audits.

Being a part of implementation of the plan, Presidential Decree No. 1438, adopted in 2010, requires that listed companies verify their financial statements in accordance with the ISA by 2015. The amendments which were made to the Law on Auditing Activity in 2013 further enlarged the scope of the ISA, by letting all companies follow the ISA.

2.3 Regulation of Accountancy Profession

The only parts of professional accountants whose work is regulated in the Republic of Uzbekistan at the state level are the auditors and chief accountants. The procedures for licensing, certification, and auditors registration are outlined in The Law on Auditing Activity No. 734-XII of 1992 as amended in 2000. This law sets up standards for applying by the profession, explains the rights and obligations of professional auditors entities, authorizing the Ministry of Finance to manage the audit activity.

The Ministry of Finance of the Republic of Uzbekistan takes responsibility, especially for the followings²³:

- 1) Certification of auditors;
- 2) Establishing requirements for professional educational programs and examinations;
- 3) Establishing continuing professional development (CPD) requirements for auditors;
- 4) Licensing and maintaining registries of licensed auditors and audit firms;
- 5) Conducting inspections of audit firms;
- 6) Suspending audit firms' licences and certificates in case of infringement of law or misconduct.

²³ <http://www.ifac.org/about-ifac/membership/country/uzbekistan>

According to The Law on Auditing Activity, professional organizations of auditors should :

- a) Participate in development of educational programs;
- b) Take part in examination procedures;
- c) Run professional examinations;
- d) Cooperate with development of laws and regulations related to Audit;
- e) Conduct mandatory ratings of audit organizations;
- f) Investigate and discipline their members;
- g) Perform quality assurance reviews of their member audit firms.

The initial professional development (IPD) requirements for the chief accountants who obliged to have their financial statements audited were introduced by the amendments to the Law on Accounting No.279-I of 1996 in 2016. If a person has a wish to be a chief accountant, he must have a university diploma and at least three years of experience in this field. Furthermore, chief accountants should undergo CPD programs which are made at least 20 hours annually. The requirements for chief accountants who provide their services to different organizations, businesses are set up by the Central Bank of the Republic of Uzbekistan and under its control. Specialists in accounting, except for auditors and chief accountants of businesses that must undergo compulsory audit, can choose a professional organization of accountants and auditors and obey their regulation. Professional organizations may provide voluntary certification programs like CAP/CIPA and the national certification of accountants, describe IPD requirements for obtaining certifications for accountants, set up CPD as well as ethical requirements, enquire and discipline their members, and perform quality assurance reviews of their members.

A voluntary national certification system of accountants was introduced by three main professional organizations of accountants and auditors in 2015:

- The Chamber of Auditors;
- The Federation of Accountants of Uzbekistan;
- the National Association of Accountants and Auditors.

The decision on certification of accountants, adopted in 2015, provides for IPD and CPD requirements for obtaining and maintaining certification and requires certification holders to be a member of a professional organization of accountants and auditors, follow the Code of Ethics and fulfill mandatory CPD requirements²⁴.

The Regulation on the Certification of Accountants which was adopted in 2015 specifies IPD and CPD requirements in order to obtain and keep the certification. According to the requirements of the regulation, holders of certification should be a member of a professional organization of accountants and auditors, fulfil compulsory CPD requirements, follow a Code of Ethics. In order to provide accounting services, an auditor does not have to have certification.

2.4 Professional Accountancy Organizations

2.4.1 The Chamber of Auditors (ChAUz)

The Ministry of Justice of the Republic of Uzbekistan established The Chamber of Auditors on August 9, 2000. It has such missions as defending auditors' professional interests and supporting the growth of their professional expertise.

As a professional organization of auditors, the Chamber has the following functions:

- Development of training programs for auditors;
- Providing the input to the legislative acts on accounting and auditing;
- Establishment of training centres for auditors;
- Development of guidance materials;
- Carrying out quality assurance (QA) reviews of its members;
- Investigation and discipline of its members;
- Conduction of conferences and seminars upon accounting matters,
- Development and promotion of the Code of Professional Ethics for auditors.

²⁴ <http://www.ifac.org/about-ifac/membership/country/uzbekistan>

Education centre at The Chamber of Auditors

The education centre for training of auditor, "AUDIT FORWARD" was established in 2000.

The main purpose of its activity is training and retraining of specialists in the field of audit, accounting and taxation. Teachers there are practising experts in the field of audit, accounting, taxation and business law, doctors and candidates of economic sciences of universities, leading experts of financial and tax authorities.

The courses taught at the education centre are:

- Training of auditors
- Professional development courses for certified auditors
- Professional development of internal auditors
- Tax advisors
- Professional development of tax advisors.

In 2017 ChAUz united 43 audit organizations and 198 auditors.²⁵

ChAUz is a member of IFAC.

2.4.2 The Federation of Accountants of Uzbekistan (FAU)

The FAU was founded in March 2014 in order to unite accountants in business. Formerly it was known as Federation of Accountants, Auditors and Consultants. Corresponding to the Chapter of FAU, its main purposes are:

- To help with the development of the accounting profession;
- To adopt and implement international standards.

The FAU is not within the members of IFAC.

²⁵https://gazeta.norma.uz/publish/doc/text139232_otchet_o_deyatelnosti_palaty_auditorov_uzbekistana_za_2017_god

2.4.3 The National Association of Accountants and Auditors (NAAA Uz)

One of the oldest professional organizations in the Republic of Uzbekistan, The NAAA Uz was established in 1992. This association unites accountants and auditors. The mission of NAAA Uz is to provide an assistance in developing of the accountancy profession and the adoption and application of international standards. The mandatory functions of NAAA Uz are:

- To assist its members, conducting educational and continuing professional development programs,
- To investigate and discipline its members;
- To keep a quality assurance review program for its member audit firms;
- To provide consulting services;
- To propose the regulator on the accounting and auditing legislation

The number of NAAA members as of December 2017 is more than 4500, including 1914 CAPs and 67CIPAs.

Education centre at The National Association of Accountants and Auditors

The education centre at The National Association of Accountants and Auditors provides an opportunity to study International certification courses for accountants and auditors. The courses includes Financial Accounting, Management Accounting, Tax and Law, Financial Management, Audit and IT (Information Technology)

Furthermore, the education centre offers the additional courses, such as Up-to-date business accounting, Advanced training courses for professional accountants and auditors, Courses of audit for beginners (after these courses people have the audit licence of the Ministry of Finance of Uzbekistan), Computer literacy (MS DOS, WINDOWS'95, WINDOWS' 97, WINDOWS' 2000, MS WORD, MS EXCEL, "1-C Accounting", and etc.), Computer in business accounting.

NAAA is the possessor of excelled licence on publishing and printing. It permanently produces monthly statement named "Everything required for an accountant", textbooks for CAP and CIPA, educational, normative and methodological literature, special accounting supporting forms and ledgers.

In this department they provide different types of consultations in such fields as business accounting, taxation and law.

They provide expert advice to their members, if they have any financial sanction from the state supervisory bodies, and protect their legal rights.

They also hold many specific seminars in different fields, such as²⁶:

- Methodology of Business accounting;
- Accounting and cost-benefit analysis in organizations;
- Types of taxation for organizations and individuals;
- Accounting the privatization transactions;
- Independent internal and external audit;
- Accounting and Audit in Joint stock companies.

The NAAA Uz is an Associate member of IFAC and an associated member of the Asian-Oceanian Standards Setters Group.

²⁶ <http://www.naaa.uz/index.php/en/about-us/sozdanie-i-razvitie>

International audit networks and international associations in Uzbekistan:

№	Name of audit organization	Membership in the international audit network	Membership in the international associations
International audit firms			
1	Audit organization LLC 'PraysvoterxausKupers'	PricewaterhouseCoopers International limited' August 29, 2002	
2	Audit organization LLC 'Deloitte va Touche'	'Deloitte Touche Tohmatsu Limited' December, 2002	
3	Audit organization LLC 'ERNST & YOUNG'	EY Global	
National audit firms			
1	Audit organization LLC 'MARIKON AUDIT'		Russel Bedford October, 2009
2	Audit organization LLC 'GRANT THORNTON'	Grant Thornton International from January 1, 2011	
3	Audit organization LLC 'ADAMAS KONSULTING SERVICE'		Baker Tilly International
4	Audit organization 'NAZORAT-AUDIT'" in LLC form		IAPA International association June, 2014
5	Audit organization LLC 'TSIAR-FINANS'		Geneva Group International Limited Zurich August, 2012
6	Audit organization LLC 'FTF-AUDIT'		Leading Edge Alliance (USA) September, 2013

7	Audit organization LLC 'HLB TASHKENT'	HLB International February, 2012	
8	Audit organization LLC 'AUDIT-SERVICES LTD'		International association Independent audit organization 'EuraAuditInternational'
9	Audit organization LLC 'KRESTON TASHKENT'	Kreston International 01.09.2011	
10	Audit organization 'PKF MAK ALYANS' in LLC form	PKF International Limited July, 2010	
11	Audit organization 'UHY TASHKENT' in LLC form	UHY International from 2012	
12	Audit organization LLC 'BAKER TILLY TASHKENT'	Baker Tilly International November, 2011	
13	Audit organization 'Audit-AS' in LLC form		Crowe Horwath Internatoinal
14	Audit organization in LLC form 'TRI-S-AUDIT'		BKR International Asiya Pasific Regional Group July, 2015

Table 4. List of international audit networks and international associations as of 01.01.2016²⁷

2.5 Adoption of International Standards (ISAs)

2.5.1 International Standards on Auditing

According to the Law on Auditing Activity No. 734-XII of 1992, it is mandatory for the Ministry of Finance to set and enforce auditing standards. The Uzbek National Standards of Auditing issued by the Ministry of Finance of the Republic of Uzbekistan are based on ISAs as of 2008.

The Ministry of Finance specified that in 2017 they expect to fully adopt ISA for all audits and stated it as a goal. Listed organizations have to have an audit of their financial statements according to ISA from 2015. It was introduced in the Decree of the

²⁷ https://www.mf.uz/media/file_en/audit/audit_networks_01_01_2016.pdf

President of the Republic of Uzbekistan No. 1438 adopted in 2010 as part of realization of the plan. In 2013 the Law on Auditing Activity was corrected and let all organizations to follow ISA, expanding the framework of application of ISA.

Within a World Bank's project for the bank sector of Uzbekistan the ISA were translated into Uzbek language in 2013. But in practice Russian translation of ISA is used more then Uzbek one. However, the Russian version of ISA which is in use is not clear.

For now International Standards on Auditing are partially adopted.

2.5.2 Quality Assurance

The Ministry of Finance is legally entrusted under the Law on Auditing Activity No. 734-XII of 1992 as amended in 2000 to ensure compliance with the licensing requirements, including the requirement to establish quality controls in accordance with the Uzbek National Standards of Auditing issued by the Ministry, which are based on ISA in effect as of 2008. ISQC²⁸ 1 has not been adopted by the Ministry of Finance for application in Uzbekistan²⁹.

According to the same law, passing the annual rating review conducted by professional organizations is mandatory for all auditing institutions of the Republic of Uzbekistan.

Obtaining a certificate on performing an external quality assurance (QA) review is included to the mentioned review.

In order to meet the requirements written in the law, professional entities of auditors, like the Chamber of Auditors (ChAUz), the National Association of Accountants and Auditors (NAAA Uz) and adopted ISQC 1 and created QA review systems for their members.

NAAA Uz's QA review system respond to the requirements of SMO 1. Besides it, according to its report it cooperates with a public oversight board, which has not been founded in the jurisdiction until now. Nevertheless, it is necessary to clarify the extent to which the ChAUz-managed quality review system is harmonized with SMO 1 requirements.

Currently this standard is partially adopted.

²⁸ International Standard on Quality Control

²⁹ "Uzbekistan." *IFAC*, www.ifac.org/about-ifac/membership/country/uzbekistan.

2.5.3 International Education Standards

Auditors, chief accountants of concrete organizations and auditors, who provide services to the companies controlled by the Central Bank of Uzbekistan must fulfil educational requirements. The Law on Auditing Activity No. 734-XII of 1992, as changed in 2000, gives the right to the Ministry of Finance to set up professional development (IPD) and continuing professional development (CPD) requirements for auditors. They should be implemented from the side of Ministry, universities, and professional organizations of accountants and auditors.

The Ministry of Finance runs its own training and examination program and takes responsibility for the certification. The Ministry sets up CPD requirements as well. According to the Chamber of Auditors (ChAUz) fit IES. During QA reviews they check out harmonization with the CPD requirement. There are initial educational programming, provided by the Universities, and according to ChAUz it does not comply with the requirements of IES.

Chief accountants of organizations who has to pass compulsory audits should fulfil the list of IPD requirements set up in the Law on Accounting No. 279-I of 1996, amended in 2016, and should take part in annual CPD programs. If the chief accountant provides the services to the organizations under supervision of The Central Bank of the Republic of Uzbekistan, he must fulfil the educational requirement established by the Central Bank.

Other professional accountants can choose to work in professional entity of accountants and auditors. In order to obtain voluntary certifications they should fulfil the requirements of that entity. Besides it, they are subject to mandatory CPD requirements established by the entity.

In general, at the time when some of the requirements of IES exist, the degree of aligning should be further set up.

Currently these standards are partially adopted.

2.5.4 Code of Ethics for Professional Accountants

There is no statutory requirements which make the professional accountants in Uzbekistan to follow the Code of Ethics.

As it was mentioned above, a legal requirements and regulations are set by the Ministry of Finance, and they regulate the profession of audit. In case of their absence, the national professional organizations of accountants and auditors takes responsibility to establish ethical requirements for their members.

The Chamber of Auditors (ChAUz) and the National Association of Accountants and Auditors (NAAA Uz) adopted a joint Code of Ethics for their members in 2005. The adoption was based on the IESBA Code. As a result, IESBA Code was adopted by the both institutions.

The ChAUz adopted the IESBA Code in 2011 and updating it in 2014 afterwards. At the same time NAAA Uz reports that its members adopted the 2010 version of the IESBA Code translated into Russian for application. There is no available information about the adoption of the IESBA Code by the Federation of Accountants of Uzbekistan, which is not within members of IFAC.

Currently the Code of Ethics for Professional Accountants is partially adopted.

2.5.6 International Public Sector Accounting Standards

Establishment of public sector accounting standards is under responsibility of The Ministry of Finance. *Public Financial Management Reform Strategy* has been adopted by the Ministry including the transition period to the international standards represented for 2009-2018.

Project, i.e the joint initiative between United Nations Development Project and the Ministry of Finance is reformed by the Budget System. It is an important part of the reform strategy, which focuses on bringing the National Public Sector Accounting Standards (NPSAS) in accordance with IPSAS. The growth of 12 converged NPSAS was announced upon round table presentations which took place in 2013–2014. There is no further available information.

For now International Public Sector Accounting Standards are not adopted.

2.5.7 International Financial Reporting Standards

The Law on Accounting represents basic accounting and bookkeeping requirements for all legal entities in the Republic of Uzbekistan. Banks and credit institutions are exceptions. It and authorizes the Ministry of Finance of the Republic of Uzbekistan to establish accounting standards both for private companies and state-financed organizations. National Accounting Standards adopted by the Ministry are a modified version of IFRS/IAS as they existed in 2008. Full adoption of IFRS is under consideration, however there is no defined timeline for this.

The Central Bank of Uzbekistan (CBU) establishes accounting requirements for banks and credit institutions and in 2004 the CBU adopted IFRS for application in the financial statements of entities under its supervision. The standards have not been updated to incorporate subsequent changes to IFRS. Prudential reporting rules established by the CBU also fall short of the requirements of IFRS.

IFRS (2013 edition) were translated into Uzbek by the National Association of Accountants and Auditors of Uzbekistan. However, as of 2016, the Ministry of Finance and the CBU have not yet adopted the translated IFRS, although they have recommended the use of that translation. Accountants and auditors in Uzbekistan regularly refer to the Russian translation of IFRS, for which the 2015 bound volume is available.

Current Status: Not adopted.

Based on the list of auditors, represented by the Ministry of finance, 650 persons have a certificate of qualification in Uzbekistan, as of 1.4.2017.³⁰

2.6 The position on the procedure of obtaining the qualification certificate³¹

The position on the procedure of obtaining the qualification certificate was approved by the Ministry of the Republic of Uzbekistan on September 20, 2000 Nr.68, and agreed with the chamber of auditors of Uzbekistan Nr 109/1 on September 25, 2000.

³⁰ https://www.mf.uz/media/file/audit/auditors/spisok_audit_01_04_17.pdf

³¹ <http://lex.uz/acts/611379>

The Regulation in accordance with the Law of the Republic of Uzbekistan "On Auditing" determines the procedure for the issuance, re-registration, annulment of the auditor's qualification certificate, extension and termination of its operation.

The qualification certificate of the auditor entitles the individual to provide audit services if he is a member of the audit firm, or if an agreement of a civil nature has been made with the auditor organization.

Each auditor who has a qualification certificate is obliged to pass the refresher courses in the amount of no less than 60 hours in accordance with the professional development programs approved by the Ministry of Finance of the Republic of Uzbekistan in agreement with the republican public association during each year starting from the year following the year of obtaining the qualification certificate auditors.

An auditor who has international certificate of accountant ("Certified International Professional Accountant (CIPA)", "Certified Chartered Accountant (ACCA)", "Certified Public Accountant (CPA)", or others and (or) a national certificate of a professional accountant ("Certified Professional" accountant"), can choose one of the courses: professional development of auditors or advanced training in the framework of international or national certification professional accountants.

The qualification certificate of the auditor is issued by the Ministry of Finance of the Republic of Uzbekistan, subject to the successful completion of the qualifying exam by the applicant.

The qualification exam is a means of testing the knowledge of persons applying for auditing on behalf of an audit organization.

Applicants who meet the qualification requirements defined by these Regulations are allowed to pass the qualification exam.

2.6.1 Qualification requirements

The applicant for the qualification certificate of the auditor must meet the following requirements:

1) the presence of higher economic education obtained in institutions of higher education of the Republic of Uzbekistan, or higher economic education obtained in an educational institution of a foreign state and recognized as equivalent to education in the Republic of Uzbekistan, and practical experience after graduating from an institution of higher education in the field of accounting and auditing , financial or tax control, or teaching in these areas for at least three years out of the last ten:

- or the presence after work of a higher educational institution of work experience, including part-time, as an auditor, assistant auditor, chief accountant, auditor or tax inspector for at least 5 years out of the last ten with higher non-economic education obtained in higher educational institutions of the Republic of Uzbekistan, or higher non-economic education obtained in an educational institution of a foreign state and recognized as equivalent to an education in the Republic of Uzbekistan ;

- or the presence of a scientific degree in the economic field of science obtained in the Republic of Uzbekistan or in a foreign state;

2) passing special training in training auditors in non-state educational institutions, accredited in the prescribed manner, on the basis of a training program approved by the Ministry of Finance of the Republic of Uzbekistan in coordination with the republican public association of auditors, and the availability of a document on the successful passing of the subject "Financial Accounting" under the International Financial Reporting Standards (IFRS) within the framework of international or national certification of professional accountants ("Certified International Professional Accountant (CIPA)", "Certified Chartered Accountant (ACCA)", Certified Public Accountant (CPA) ", " Certified Professional Accountant "or others) or ACCA diploma in international financial reporting.

Applicants who have an international accountant certificate or a national certificate of a professional accountant and at least two years of experience in an audit organization from the last five years on the territory of the Republic of Uzbekistan are allowed to pass the qualification examination without passing special training to train auditors in non-state educational institutions.

2.6.2 Submission materials for obtaining the qualification certificate of the auditor

The applicant for obtaining the qualification certificate of the auditor submits to the Ministry of Finance of the Republic of Uzbekistan an application for admission to the qualification examination with the following documents:

- a completed application form
- a diploma of education or a diploma of obtaining a scientific degree in the economic field of science or their copies certified by the institution that issued the document; or a certificate of an authorized state body on the approval (establishment of equivalence) of an education certificate or a degree (in the presence of higher education or a diploma of academic degree obtained at a foreign educational institution or their copies certified by the institution that issued the document ;
- employment record or its copy certified by the place of work (if you have work experience in combination with a record in the workbook);
- two photos;
- the original document on the passage of special training for the training of auditors in non-state educational institutions;
- either an international certificate of an accountant or a national certificate of a professional accountant (copies are made, originals are returned) or their copies certified by the institution that issued this document, if there are documents confirming the qualification for the last five years at a fixed frequency.
- a bank payment document evidencing the payment of a fee for processing an application for participation in a qualifying examination in a 1.5-fold minimum wage³².
- copy of passport.

³² 184 300 so'm as of July, 2018 (approx.22 USD)

2.6.3 The procedure for qualifying exams

Applicants are allowed to take a qualifying exam upon presenting a passport or other document proving their identity. Applicants who do not have a passport or other document proving their identity or who are late for the qualification examination are considered to be unavailable and transferred to the list of persons admitted to the next qualifying exam.

If the applicant within six months, starting from the date of submission of documents to the Ministry of Finance of the Republic of Uzbekistan, did not appear for the qualification exam, the submitted documents are returned to the applicant. Re-submission of documents is carried out in the manner specified in "Required submission materials for obtaining the qualification certificate of the auditor".

The qualification exam for a group of applicants (at least 10 and no more than 20 people) is conducted in two stages: testing (in writing for four academic hours, according to the results of which the applicant is admitted to the written and oral exam; written and oral exam on exam papers (three academic hours are provided for solving problems and preparing for an oral answer). Both stages of the qualification exam for one day are not allowed.

Tests, exam questions and correct answers are developed by the Ministry of Finance of the Republic of Uzbekistan in cooperation with the Republican public organization of auditors on the basis of the Auditor Training Program.

Forms of tests and examination tickets without the signature of chairman of the examination committee are considered invalid. The content of the tests and examination tickets, taking into account the amendments and additions made to the laws and regulations, is periodically reviewed.

Testing includes at least 75 questions that reflect all sections of the program. The number of correct answers, which is the basis for the recognition of test results as positive, must be at least 75% of the number of questions contained in the examination tests.

If the test results are recognized as negative, the applicant is not allowed to pass the written-oral exam, and the submitted documents are returned to him.

The examination ticket consists of four parts, each of which includes a theoretical question and a practical task in the following disciplines:

- a) First part - financial Accounting;
- b) The second part - management accounting, financial management and financial analysis;
- c) The third part - audit;
- d) Fourth part - taxation and legal regulation of business activities.

Answers for each of the four parts of the examination ticket (including the solution of the problem) are evaluated on a five-point system. Successfully passed the exam are applicants who have received at least 15 points on the exam ticket.

During the qualification exam to use legislative and instructive material, reference and special literature, to negotiate with other applicants is prohibited. Applicants who violate these requirements are removed from the audience and are considered not to have passed the qualification exam.

Unauthorized persons and observers are not allowed to attend the qualification exam.

After the time allotted for the testing, applicants are required to pass tests and answers to the examination committee. Applicants who violate these requirements are considered not to have passed the qualification exam. The results of the qualification exam are announced by the examination committee not later than two days after it.

The results of the qualifying examination are drawn up by the protocol of the examination board and are transferred to the Ministry of Finance of the Republic of Uzbekistan within 3 days after the date of the qualification examination.

Written works of applicants for passing the qualification examination (tests, tickets and answers to them), as well as protocols of examination commissions are kept in the Ministry of Finance of the Republic of Uzbekistan in the established order.

The fee is not refundable for applicants (auditors) who have not passed the qualifying exam.

An applicant (auditor) who has not passed the qualifying exam has the right to re-submit in the prescribed manner documents for obtaining a qualification certificate, but not earlier than one month from the date of participation in the qualification exam, subject to payment of a fee for issuing a qualification certificate.

3. Ethics as part of audit profession. Independence as core issue of auditors ethic

3.1 Ethics and moral

The word "ethics" can be often heard in audit profession. Before getting into audit ethics, I would like to mention what ethics actually mean and what it represents.

The Ethics (greek "ἠθικόν", from ancient greek "ἦθος"- ethos, "disposition", "custom") - is a philosophical discipline, the subject of which is morality. Ethics is inseparable from the philosophy from the time of its inception.

This terminology was first used by Aristotle as a indication of a special field of investigation of "practical" philosophy, and it tries to answer the question: what should we do?

Aristotle called happiness the main goal of moral - the activity of the soul in the fullness of the virtue, that is, self - realization. Self - realization of a person is a rational act that avoids extremes and is held in the golden mean. Therefore, the main virtues are moderation and prudence.

According to Aristotle, who was taught by Platon, the goal of ethics is not knowledge, but deeds. The question of what is good in ethics is related to the question of how to achieve it. In this way, ethics as a practical philosophy was separated from theoretical philosophy (metaphysics).

Happiness is usually called the highest good. Happiness needs external blessings and luck, but it mainly depends on the perfect activity of the soul - from activities consistent with virtue. The property of the soul to act in accordance with the virtues, according to Aristotle, continues the subject of ethics. In the broad sense of ethics in Aristotle - the science of the policy (political science), which sets the basis for politics and for the economy.³³

³³ Введение. О предмете этики // Этика. Под ред. А. А. Гусейнова, Е. Дубко.

The so-called "golden rule of ethics"-"do not do to others what you do not want yourself"- existed in one form or another independently in different cultures. It is present in Confucius³⁴, occurs in the Mishnah³⁵.

Some people may confuse the ethics and moral. However, it should be mentioned that there are some differences between those concepts.

Moral is originated from latinos "mós" which means custom, manner. It also represents the way of life of individual person and his or her personal characteristics.

Morality is one of the ways to regulate people's behavior in society. It is a system of principles and norms that determine the nature of relations between people in accordance with the accepted in the society concepts of good and evil, fair and unjust, worthy and unworthy. Compliance with the requirements of morality is ensured by the power of spiritual influence, public opinion, inner conviction, the conscience of men.

"Morality is not the doctrine of how we may make ourselves happy, but how we may make ourselves worthy of happiness". – Immanuel Kant³⁶.

3.2 Business ethics

Every economic activity has ethical measurement. Even if to look at some basic economic transaction in the simplest form, the ethical dimension can be observed. In business transactions two parts cooperates to exchange the goods and services for money. One side gets the good or service what he wants and the second part receives the money. In case of fair exchange both of them benefit and in this way both sides' interests are served. It can lead to the future cooperation between partners. In this kind of transaction both parties are satisfied and it is good not only for one, but for two of them at the same time.

Of course, these business transactions can go in a terribly wrong way. For example, if the seller charges an unfair price, provides the product or service with lower quality than buyer expects, or if the good does not reach the customer, or if the buyer refuses to

³⁴ Конфуций. Беседы и суждения. — [15:24](#), [12:2](#), [5:12](#)

³⁵ Шабат, 31a

³⁶ <https://everydaypowerblog.com/immanuel-kant-quotes/>

pay the agreed amount of money or to pay at all and so on. Those situations are only a few examples that can occur in business transactions.

Business ethics focuses on what is good and right in economic activity³⁷. Moral analysis and evaluation of economic practices and activities includes business ethics. This moral assessment can be done in three levels:

1. The level of economic system (macro-economic level);
2. The level of organization (meso-economic level);
3. The level of intra-organization (micro-economic level).

The level of economic system (macro - economic level). On this level of assessment, business ethics measures economic systems, macro - economic policies and trade - agreements to define if they are fair and proper. This level refers to the policy framework in which economic exchange happens. At national level, this framework is defined by the political power of the country.

Any economic policy has an impact on the people. They might be established to give people more freedom or to meet a specific social or political purposes like protecting poorest people in society. The objectives can be different. But anyway, these economic systems or policies have positive or negative consequences for people.

According to the opinion of Adam Smith, the father of capitalism, capitalism is the system that would best serve the well-being of society. Karl Marx, who opposed capitalism and suggested capitalism instead, denied capitalism on moral sides and defended socialism. He believed that socialism could be the best system for everyone in society.³⁸

The level of organization (meso - economic level). This level concerns the business organizations, like corporations or companies, and their relationship with society. Business organizations have an influence on people, like on their clients and suppliers. Beside this, those organizations can influence local communities, local culture and natural environment. Based on the operations of the companies, influences can be either beneficial or detrimental. Many questions raises from this. People need to know if

³⁷ Ethics for accountants and auditors. D.Rossouw., F.Prinsloo , Ch. Du Plessis. 2009

³⁸ Ethics for accountants and auditors. D.Rossouw., F.Prinsloo , Ch. Du Plessis. 2009

the business should take the responsibility for its influence on society, or if the government should control the businesses to make sure that they do not harm society and natural environment.

The ethical impact that business has on society is studied at this level of business ethics.

The level of intra - organization (micro - economic level). This level of business ethics refers to economic activity within organizations. It focuses on the moral sides of business practices, behavior, policies and decisions that take place within an organization.

Business organizations have an impact on people who work in this organization. Quite often employees and managers come up to moral problems in different cases that arise at work. Working conditions can cause a risk to the physical and mental health of employees. The organizational culture, policies, rules or systems can be such that it cracks down the trust between the employees within the organization.

Relations at work are ethically charged within the organizations. These kinds of situations have an impact on people and the quality of peoples' live is often determined by it. Due to the effects of those situations on society, business ethics on intra - organization (micro - economic level) level should be studied as well.

3.3 Ethics and the law

There are many ideas about the relationship between law and morality. Supporters of the theory of natural law insist on the need to connect the law and morality, because they believe that the law ceases to be the law if it violates natural law. On the point of view developed by Lon Fuller³⁹, there is a need to connect the law and morality, although this negates the need for the moral content of the law and brings to the fore the idea, or concept of law.

As for G. Hart, who represents the third point of view, he actually denies the need for such a connection. Different political theories may require different options for

³⁹ https://en.wikipedia.org/wiki/Lon_L._Fuller

combining law and morality. If there are different concepts of morality, then the relationship of law and morality will change depending on the latter.

As for G. Hart, who represents the third point of view, actually denies the need for such a connection. Different political theories may require different options for combining law and morality. If there are different concepts of morality, then the relationship of law and morality will change depending on the latter.

Ethics raise the following questions:

- 1) Does a person have a moral obligation to obey the law?
- 2) Are there conditions under which a person has a moral right or moral obligation not to obey the law?
- 3) Can something immoral under certain conditions also become lawless?
- 4) Should the law be used to achieve moral goals?
- 5) Should law or legal systems be evaluated from a moral point of view?

There is much in common between ethics and law. They represent the value forms of consciousness, have a normative content and serve as regulators of human behavior. Ethics and law are determined by social, political and economic factors of social life. They have a common goal - to harmonize the interests of the individual and society, to strengthen the freedom and dignity of the person, to preserve public order. Ethics and law are guided by the ideals of freedom and justice.

At the same time, ethics and the right have a significant difference. Morality was formed even before the division of society into classes and the formation of the state. The right expresses the will of the state, the legal consciousness of the people. The principles and norms of morality are rooted in the public consciousness. They are supported by lifestyle and art. The right expresses the will of the state and the people and does not always provide a choice of behavior. It is basically its directive.

The sphere of morality is wider than the sphere of those relations that are determined by legal consciousness. The private, family life of people is subject to moral judgment, not

legal regulation. Legal rules are always very specific, protocol and do not leave room for free interpretation. They indicate the state approach to the assessment of specific social relations. Moral requirements have a broader meaning and allow to interpret and apply these requirements in different ways. For example, morality rejects all types of deception and lies, while the right pays attention only to certain types of deliberate deception.

The norms of morality are performed by virtue of personal conviction, human habits. The internal guarantor of morality is conscience, and external - public opinion. "My conscience means more to me than all speech", Cicero asserted⁴⁰.

3.4 Professional ethics for auditors

3.4.1 Reasons to study ethics

While learning the ethics in auditing, one simple question might come to our mind: why, actually, auditors should study ethics?.

Of course, each auditor has some moral beliefs that he follows. However, there are several reasons to study ethics. Some of them are:

- 1) Some beliefs of auditors might be not enough, because they are simple beliefs about complex problems. The study of ethics can help to figure out what principles operate in those issues.
- 2) The study of ethics helps to develop ethical reasoning skills.
- 3) Some beliefs of individuals may be inadequate or they may cling to inadequate values. Learning those beliefs and values by critical analysis can show their inadequacy.
- 4) Another important reason to study ethics is to learn why and if our opinions are worth holding.
- 5) And one more reason in to identify the basic ethical principles that auditors can apply to action.

⁴⁰ [https://studme.org/52685/etika i estetika/etika pravo](https://studme.org/52685/etika_i_estetika/etika_pravo)

3.4.2 Auditor independence

The main objective of an audit is to provide company shareholders and creditors with an proper, expert and independent opinion on to if the annual financial statements of the company illustrate a fair and true view of the financial condition of the entity and if they are reliable. Independence is the primary indicator by which an auditor shows that he can objectively perform his task.

Independence is defined as follows:

- a. "Independence of mind is the state of mind that permits a member to perform an attest service without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional scepticism.
- b. Independence in appearance is the avoidance of circumstances that would cause a reasonable and informed third party, who has knowledge of all relevant information, including safeguards applied, to reasonably conclude that the integrity, objectivity, or professional scepticism of a firm or member of the attest engagement team is compromised."⁴¹

The auditor, who provides professional services to an entity, for which independence is required in fact, which means independence of mind and independence in appearance, as it is reflected in the definition.

3.4.3 The necessity for auditor independence

The opinion of the auditor should not be influenced by the relationship between him and the client company to which he provides the service. The auditor should act independently from that company. Shareholders expect to receive from the auditors a true and honest opinion on the financial statement.

⁴¹<https://www.aicpa.org/interestareas/professionalethics/resources/tools/downloadabledocuments/plain%20english%20guide.pdf>

Sometimes doubts are expressed regarding the independence of external auditors. It can be discussed that if proper corporate governance measures are not taken, the auditing firm can come to audit opinions and judgments that are highly influenced by the desire to keep good relations with the client company. Shareholders can not rely on the opinion of the auditor, and he can not be considered as an independent, if it happens.

Accounting and audit firms sometimes establish audit fees below market rate and compensate for the deficit by providing non-audit services such as management advice and tax advice. As a result, some audit firms also protect commercial interests. This raises ideas that the interests of the auditor to protect the shareholders of the company and its commercial interests may be contradictory.

A large profile example could be the relationship between Enron and their auditors, Arthur Andersen. In 2000, Andersen received \$27m for non-audit services, compared with \$25m for audit services, meaning Enron accounted for over 25% of the fees generated by the firm's Houston office. In the aftermath of Enron's demise, the accounting firm was accused of not acting independently and suggestions were made that they had gone along with the accounting practices in Enron in order to retain their work⁴².

3.4.4 Threats to auditor independence

There are some threats to auditor independence that were recognised by the audit profession. Many of those threats are linked to the provision of non-audit services. The followings are the examples of the main threats:

- 1) Self-interest threat. When an auditor depends financially on the client company or somebody closely associated with him is financially interested in that client. The auditor can also depend on company management to ensure that he will be re-appointed as an auditor.
- 2) Familiarity threat. The auditor and the client have long-lasting relationships, or they know each other so well that the auditor starts to give advice or act as a manager.

⁴² <http://www.corplaw.ie/blog/bid/369348/Importance-Of-Auditor-Independence>

- 3) Self-review threat. A judgment is required of the auditor who demands that previous work of the company be challenged or re-assessed.
- 4) The trust threat. When the auditor starts trusting the directors or management too much. It prevents proper auditing of management representations and information.
- 5) The intimidation threat. It can happen when the client or other party intimidate the auditor by actual or potential.
- 6) The advocacy threat. When the auditor becomes engaged in actively promoting or protecting the interests of the client.

Because of some rules, the audit can not be conducted by:

- 1) Audit organizations whose heads and other officials are the founders (participants) of the audited persons, their officials, accountants and other persons responsible for organizing and maintaining accounting records and drawing up accounting (financial) statements;
- 2) Audit organizations whose leaders and other officials are in close relationship (parents, spouses, brothers, sisters, children, as well as brothers, sisters, parents and children of spouses) with the founders (participants) of the audited persons, their officials, accountants and others persons responsible for the organization and maintenance of accounting and preparation of accounting (financial) statements;
- 3) Audit organizations in relation to the audited persons who are their founders (participants) in relation to the audited persons for whom these audit organizations are the founders (participants) in respect of subsidiaries, branches and representative offices of these audited persons, as well as in relation to organizations having
- 4) Common with this audit organization of founders (participants): audit organizations, individual auditors who have provided services for the restoration and maintenance of accounting, as well as the preparation of accounting (financial) reports to individuals and legal entities for these persons during the three years immediately preceding the audit;

5) The auditors who are the founders (participants) of the audited persons, their managers, accountants and other persons responsible for the organization and maintenance of accounting and the preparation of accounting (financial) statements;

6) Auditors who are with the founders (participants) of the audited persons, their officials, accountants and other persons responsible for organizing and maintaining accounting records and drawing up accounting (financial) statements in close relationship (parents, spouses, brothers, sisters, children, as well as brothers, sisters, parents and children of spouses).

Systematizing the given reasons, it can be concluded that when conducting a mandatory audit, auditors should not be dependent on the company being audited in the following ways:

- Financially (materially);
- With relationships (with persons responsible for the organization and maintenance of accounting and financial reporting);
- Officially.

The procedure for payment and the amount of monetary remuneration to audit organizations and individual auditors for conducting an audit (including mandatory) and the provision of related services are determined by the contracts for the provision of audit services and cannot be made dependent on the content of the findings of the audited persons that can be made as a result of an audit.

Thus, the auditor is obliged to closely monitor that the principle of independence is not violated at all stages of the audit, and to take the necessary measures to eliminate the circumstances that have arisen. In the event of the establishment of the facts testifying to the loss of independence and the impossibility of eliminating the relevant circumstances, it is necessary to refuse to conduct an audit.

Independence of the auditor is one of the principles of the audit, which consists in the absence of a financial, property, kindred or any other interest on the audited economic entity, exceeding the relations under the contract for the implementation of audit services, as well as any dependence on the auditor third party, owners or managers of the audit organization in which the auditor works.

In the conclusion or other document drawn up as a result of the professional services rendered, the auditor is obliged to consciously and without any reservations to declare its independence in relation to the client, both in formal and in factual circumstances.

3.5 Audit quality and value adding effect

The auditors have an important role in the well-being of the organizations. The higher quality their work is the higher they are appreciated. The auditors have a potential to be highly valued and the following example is about value adding effect of audit quality.

Two companies A and S operate in the same industry. Both have the same assets and liabilities, risk profile and cash flow characteristics. Being economically identical, those two companies have the same competencies, the same management qualities and the same competencies. In the given example, the company A is audited by competent and independent auditor. The company B does not have an audit. Which company would have higher stock price if they were traded in stock exchange? The answer would be company A. This is implicit answer. The reason A company's stocks being highly valued is that the information given to the market has "information risk".

The example can be extended by adding two identical companies: one company was audited by an audit firm that is famous for high quality audit services and has good reputation. The second company was audited by the audit firm that has a reputation for providing an adequate audit. There will be a difference in the stock prices of those companies. That difference will not be as large as that existing for companies with a competent, independent audit and no audit at all, but will exist anyway, even if other things will be equal.

So the conclusion is different audit quality levels have different value adding effects.

Furthermore, what is more important, that the quality difference in the audit turns into the difference in the prices of shares traded on the stock markets.

4. New approach to Code of Ethics IEAASB⁴³ (IFAC⁴⁴). Comparison with previous legal regulation

4.1 The International Code of Ethics for Professional Accountants

In the April 2018, a fully completely rewritten and revamped Code of Ethics for professional accountants (PAs) was released by the IESBA⁴⁵. The name was changed into "International Code of Ethics for Professional Accountants/including International Independence Standards". The Code will become effective on June 15, 2019.

It includes all main advancements in terms of ethics and independence for the last four-year period in one document. It also contains the new provisions regarding non-compliance with law and regulations ("NOCLAR"), which was already valid since July 2017 and reviewed independence provisions regarding the long association which will be effective from December 2018.

More than 120 jurisdictions and Forum of Firms⁴⁶ has adopted the earlier version of the Code⁴⁷.

4.1.1 The major areas of focus

The primary principles in the Codes are:

- Integrity;
- Objectivity;
- Professional competence and due care;
- Confidentiality and professional behavior.

The principles set the behavioral standard expected from professional accountant (PA) and it represents the recognition of profession of its public interest responsibility.

Those primary principles and the categories of threats to them, such as self- review, self-interest, familiarity, advocacy and intimidation threats remain unchanged.

⁴³ The International Auditing and Assurance Standards Board

⁴⁴ The International Federation of Accountants

⁴⁵ International Ethics Standards Board for Accountants

⁴⁶ The Forum of Firms is an independent association of international networks of firms that perform transnational audits.

⁴⁷ <http://www.ethicsboard.org/revised-and-restructured-code-ethics>

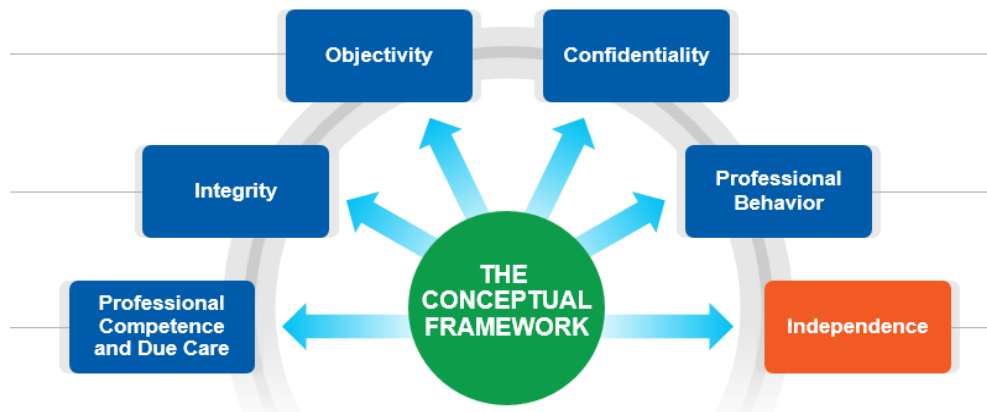
Also, the overarching requirements for applying a conceptual framework for adhering to fundamental principles and, if applicable, being independent are also unchanged.

Besides the structural revisions made to the entire Code of ethics, the substantive revisions contain⁴⁸:

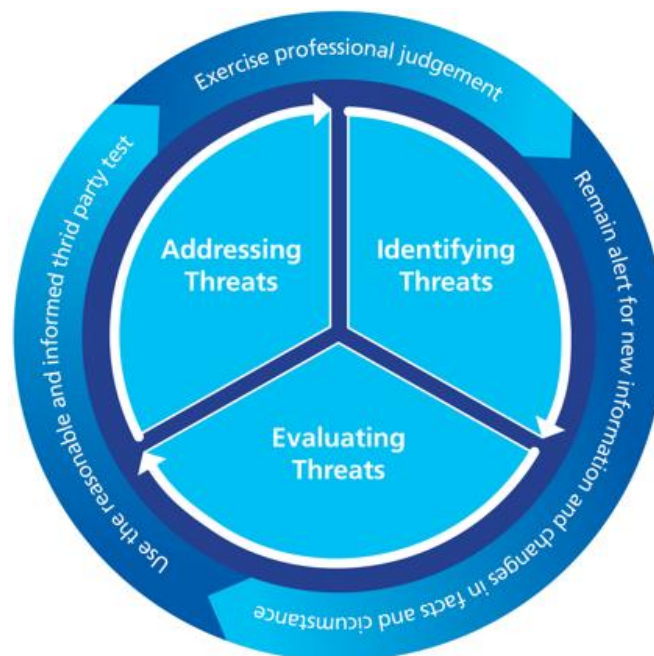
- 1) An improved conceptual framework, that includes broad revisions to "safeguards" throughout the Code that are better aligned to threats;
- 2) Consolidated independence provisions related to long association of personnel with audit clients;
- 3) Consolidated provisions regarding the offering and accepting of inducements, including presents and hospitality which apply to both PAs in business ("PAIBs") and PAs in public practice ("PAPPs");
- 4) Strengthened provisions devoted to PAIBs, including:
 - A new part regarding the pressure to breach the primary principles;
 - Revised provisions regarding the preparation and presentation of information.
- 5) Clarifications about the applicability of PAIB provisions to PAPPs;
- 6) New material to accent the importance of understanding facts and conditions when exercising professional judgment;
- 7) New material to explain how compliance with the primary principles supports the implementation of professional scepticism in an audit or other assurance engagements.

⁴⁸ "The International Code of Ethics for Professional Accountants: Key Areas of Focus for SMEs and SMPs." *IFAC*, www.ifac.org/global-knowledge-gateway/ethics/discussion/international-code-ethics-professional-accountants-key.

Strengthened conceptual framework:



Pic.1. The conceptual framework.⁴⁹



Pic.2. Dealing with threats.⁵⁰

The conceptual framework represents a set of principles-based provisions in Section 120, The Conceptual Framework of the Code that all PAs are required to apply to deal with ethics and independence issues. It applies to all PAs and defines a three-step approach that includes identification, evaluation and addressing threats to be in accordance with the fundamental principles and, if applicable, independence.

⁴⁹ http://www.ifac.org/system/files/uploads/gateway/Ethics_photo_1.png

⁵⁰ https://www.ifac.org/system/files/uploads/gateway/Ethics_photo_2.png

Comprehensive review have been made to the conceptual framework to reinforce and clarify how all PAs need to identify, evaluate and address threats to the fundamental principles and if applicable, be independent. SMPs⁵¹ should take note of the explanation of how PAs should deal with threats, including the new requirement for PAs to "stand back" and consider if overall conclusion made or actions they have taken are appropriate to resolve the problem.

In response to concerns from the regulatory community that some safeguards were not specific or effective enough, the strengthened conceptual framework now has a more clear definition of safeguards which is "actions, either individually or in combination, that a PA takes that effectively reduce threats to compliance with the fundamental principles to an acceptable level". It is no longer a valid notion that all threats can be addressed by the application of safeguards⁵².

The strengthened conceptual framework explains that in certain conditions, the PA may not have any other option but to decline, or finish the specific professional activity, or service.

The strengthened conceptual framework emphasizes that threats are addressed in two ways⁵³:

- a) by eliminating the conditions that create the threats; applying safeguards where they are available or are able to reduce the identified threats to a reasonable level;
- b) by declining or finishing the specific professional activity or service.

Particularly, SMPs should note the difference between safeguards and "conditions, policies and procedures" which are in contrast routine in nature and can help the PA in identifying and assessing threats. It is clarified in the conceptual framework that the conditions, policies and procedures established by profession, legislation, regulation, the firm, or the employing entity to strengthen PAs acting ethically are not safeguards as they are not specifically designed to deal with a given threat. Clearer descriptions and

⁵¹ Small and medium size practices

⁵² "The International Code of Ethics for Professional Accountants: Key Areas of Focus for SMEs and SMPs." *IFAC*, www.ifac.org/global-knowledge-gateway/ethics/discussion/international-code-ethics-professional-accountants-key.

⁵³ <https://www.ifac.org/global-knowledge-gateway/ethics/discussion/international-code-ethics-professional-accountants-key>

definitions of other main terms like "reasonable and informed third party (RITP)" and "acceptable level" are set, and a new term "appropriate reviewer" was introduced. It is explained by the new Code that a RITP test is a term which includes consideration by a PA about if another party would reach the same conclusion (i.e., RITP). The RITP test is made from the point of view of the RITP and involves weighing all related facts and conditions that the PA knows or may reasonably be supposed to know at the time when the conclusions are made. A RITP does not have to be a PA, but needs possess related knowledge and experience to understand and assess the appropriateness of the PA's conclusions in a fair manner. The reviewed description of reasonable level in the enhanced conceptual framework is more closely connected with the term of RITP test and clarifies that it is the level at which a PA applying the RITP test would likely conclude that the PA complies with the basic principles.

The expanded conceptual framework more clearly indicates the requirement that all PAs remain vigilant for new information or changes in facts and circumstances when applying the conceptual framework. It is also explained there, that when a PA gets new information or becomes aware of changes to facts and circumstances that might influence if a threat has been eliminated or decreased to an acceptable level, the PA needs to evaluate and address that threat in accordance with that. The new conceptual framework also stresses that PAs should exercise professional judgment and apply the concept of the RITP test in all three stages of using the conceptual framework.

In the end, the enhanced conceptual framework contains new application material to clarify that firms and network firms should use the conceptual framework to recognize, assess and address threats to independence.

In response to questions about responsibilities of firms for independence, the Code refers to the International Auditing and Assurance Standards Board's (IAASB) ISQC 1 standard which require firms to set policies and procedures for complying with independence.

4.2 The use of the Conceptual Framework regarding Non-Assurance Services

SMPs need to take note of changes in independence clauses related to the provision of non-assurance services (NAS) for auditing and assurance clients. Substantial changes were made to better explain how firms and network firms should apply a conceptual framework to deal with threats to independence created when a NAS is provided to audit and assurance clients.

The prohibitions in the Code regarding NAS are more noticeable, including a comprehensive prohibition related to the adoption of management responsibilities, which is used in the provision of all types of NAS to audit clients. In addition, it is now clear which NAS provisions apply in all cases; and which one is used to audits of entities that are objects of public interest entities (PIEs); versus audits of non-PIE organizations.

In accordance with the new description of safeguards in the conceptual framework examples of actions that can be safeguards in the NAS section of new Code are much clearer and more closely related to a specific category of threats.

The Code explains that in certain cases, safeguards are unavailable or can not reduce the threats that are created by providing NAS to audit clients to an acceptable level, and that if this kind of threats cannot be eliminated, the firm or network firm has to decline or finish the NAS or the audit involvement⁵⁴.

⁵⁴ “The International Code of Ethics for Professional Accountants: Key Areas of Focus for SMEs and SMPs.” *IFAC*, www.ifac.org/global-knowledge-gateway/ethics/discussion/international-code-ethics-professional-accountants-key.

The prohibitions for providing of non-assurance services in Regulation
(EU) No 537/2014 of the European parliament and of the council and in the
New Code of Ethics:

Regulation (EU) No 537/2014 of the European parliament and of the council⁵⁵	New Code of Ethics⁵⁶
- tax services (preparation of tax forms, payroll tax, customs duties, provision of tax advice...);	- Tax services; - Certain types of tax services;
- bookkeeping and preparing accounting records and financial statements;	- Accounting and bookkeeping services; - Accounting and bookkeeping services such as preparing accounting records and financial statements, including those NAS of a routine or mechanical nature provided to divisions or related entities;
- valuation services, including valuations performed in connection with actuarial services or litigation support services;	- Valuation services; - Valuation services, including tax services involving valuation;
- legal services, with respect to: (i) the provision of general counsel; (ii) negotiating on behalf of the	- Legal services;

⁵⁵ A statutory auditor or an audit firm carrying out the statutory audit of a public-interest entity, or any member of the network to which the statutory auditor or the audit firm belongs, shall not directly or indirectly provide to the audited entity, to its parent undertaking or to its controlled undertakings within the Union any prohibited non-audit services in:

(a) the period between the beginning of the period audited and the issuing of the audit report; and (b) the financial year immediately preceding the period referred to in point (a) in relation to the services listed in point (g) of the second subparagraph.

⁵⁶ includes an overarching requirement that prohibit firms and network firms from assuming management responsibilities when providing NAS to audit clients; and specific requirements to prohibit certain types of NAS either in all circumstances; or in certain circumstances

audited entity; and (iii) acting in an advocacy role in the resolution of litigation;	
- services related to the audited entity's internal audit function;	- Internal audit services; - Services related to the audited entity's internal audit function;
- services linked to the financing, capital structure and allocation, and investment strategy of the audited entity, except providing assurance services in relation to the financial statements, such as the issuing of comfort letters in connection with prospectuses issued by the audited entity;	- Corporate finance services; - Services linked to the audited entity's financing, capital structure and allocation, and investment strategy;
Others: - services that involve playing any part in the management or decision-making of the audited entity; - payroll services; - designing and implementing internal control or risk management procedures related to the preparation and/or control of financial information or designing and implementing financial information technology systems; - human resources service, with respect to: (i) management in a position to exert significant influence over the preparation of the accounting	Others: - Administrative services ; - Information technology (IT) systems services; - Litigation support services; - Recruiting services; - Designing and implementing IT systems, internal control or risk management procedures; - Litigation support services when used for the purpose of advancing the entity's interest in a legal proceeding or investigation with respect to amounts that are material to the financial statements subject to audit or review.

records or financial statements which are the subject of the statutory audit; (ii) structuring the organisation design; and (iii) cost control.	
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Table 5. The comparison of prohibitions in of non-assurance services in Regulation (EU) No 537/2014 of the European parliament and of the council and in the New Code of Ethics.

4.3 Provision of Recruiting Services to Audit Clients

The new description of recruiting services and clarification of the types of recruiting services that firms and network firms are banned to provide to their audit clients are established in the Code.

One of those bans is related to seeking for, or searching after the candidates and undertaking reference checks of prospective candidates for directors or officers of the organization, and senior management in a position to exert great influence on the matters of the clients which is now extended to all organizations. It no longer applies to only audits of entities that are PIEs, unlike the extant Code. The reason was, that the IESBA has mentioned that there are no available safeguards to cope with the familiarity and self-interest threats that are created by providing this kind of recruiting services to audit clients in general.

4.4 Long association

In December 2017, the changes to independence provisions regarding long association of personnel with an audit or assurance has been finished by IESBA. It contains several substantive enhancements, including strengthened partner rotation regime for audits of public interest entities.

The reviewed long association provisions were made especially according to the structure and drafting conventions of previous edition of the Code of Ethics for Professional accountants (from 2016) and it set out in January 2017 close-off document. Those revisions will be effective from December 2018.

In the end of the renewed Code, the IESBA made restructuring and corresponding safeguards-related revisions to the long association provisions. But the substance of the long associations was not changed by this.

4.5 Inducements

The revised inducement provisions were released by the IESBA, a few months after the release of renewed and restructured Code, in April 2018. Those provisions help to clarify the meaning of inducement and guides the behaviors of PAIBs and PAPPs in every case including inducements.

Complementing the provisions of NOCLAR, which were effective since July 2017, the revised incentive provisions offer a complete system of ethical protections which are connected both with participation of PAs in potentially unethical behavior or official crimes made by other people. They make the last fragment of the restructured and renewed Code, and will be also valid from June 2019.

4.6 Clarification about Applicability of PAIB Provisions to PAPPs

According to the opinion of IESBA, PAs and firms that provide professional accounting services may face similar problems and ethical dilemmas as professional PAIBs. That is why, in finalizing the restructured Code, the IESBA set a new requirements and application material to make clarification that Part 2 of the Code can be relevant to PAPPs when they do professional activities in accordance with the relationship with the firm, whether as an owner, employee or contractor of the firm. SMPs need to take into count different examples presented in Part 3⁵⁷ of the Code to show the examples of such situations.

4.7 Professional Judgement

With regard to professional judgment, the Code emphasizes its importance in identifying, evaluating and eliminating threats in order to make informed decisions and

⁵⁷ Part 3 – Professional Accountants in Public Practice

gain an understanding of specific facts and circumstances, including the nature and scope of the professional activity or service; and interest and relationships included. The IESBA has added new material to the Code to help PAs better understand what to consider in practising professional judgement. For instance, the Code clarifies that within other matters, practising professional judgement includes a consideration of if:

- There is a reason to fear that potentially relevant information could be missing from the facts;
- There is an inconsistency between the circumstances and known facts and PA's expectations;
- The examination of PA and experience are enough come to conclusion;
- There is a need for consultation with others having relevant examination and experience;
- There might be other rational conclusion that could be reached from the given information.

The new material regarding professional judgement designed to make more obvious procedures that PAs should already be doing under the extant Code and is expected to guarantee that PAs exercise professional judgement in a more consistent way.

4.8 Restructuring Changes

Besides the more substantive revisions, the Code involves different structural revisions that help to make it more user-friendly. The requirement paragraphs are identified by the letter "R", while the application material that clarifies those requirements are generally included in the next paragraph, identified by the letter "A".

The Code has clearer language now. The IESBA avoided duplication material, where possible, simplified complex sentences, avoided passive voice, legalistic and archaic terms.

The new structure and formation of the Code sets a new architecture that emphasizes the Code's scalability.

4.9 Guide to the Code

There is a Guide to the Code, created by IESBA, which accompanies the Code. It helps the readers to better understand the purpose of the Code, the way how it is structured and how to use it.

Being non-authoritative, the Guide does not form part of the Code itself. SMEs⁵⁸ and SMPs are recommended to learn the Guide as this will definitely help them navigate the different parts and sections of the Code, including the International Independence Standards.

4.10 To Recap

The Code derives from the completion of a several substantive IESBA projects, including the Structure of the Code, Safeguards, and Revision of Part C. It also involves recently completed projects – R and Long Association.

The restructured and reviewed Code is responsible to long-standing concerns about the Code. It also⁵⁹:

- Answers to fears that the biggest barrier faced by SMPs in complying with the existing Code is connected to a lack of a full understanding of its requirements.
- Addresses problems raised by regulators and the PIOB about the robustness of particular provisions in the Code and its overall enforceability.
- Sets an integrated set of ethics and independence provisions that are easier to apply, navigate and impose.

The IESBA's work on each kind of project has been actively monitored by the SMP. The SMP has provided input and suggestions focusing on matters that impact SME and SMP's constituents.

The IESBA is planning to introduce a period of stability next after the launch of the Code and have committed that there will be no further changes that will become effective before June 2020.

⁵⁸ Small and medium sized entities

⁵⁹ "The International Code of Ethics for Professional Accountants: Key Areas of Focus for SMEs and SMPs." *IFAC*, www.ifac.org/global-knowledge-gateway/ethics/discussion/international-code-ethics-professional-accountants-key.

The new code is also a principle-based and in comparison with previous ones. New Code of ethics is fully re-written, restructured code to strengthen the clarity and contains many lots of important revisions.

The new Code includes clear differences between requirements and application material, it provides with much more prominence on basic principles, the conceptual framework and the requirements related to the independence of PAs.

In fact, the reviewed Code is now much clear, much easier in usage, in application, and translation.

The restructured Code includes:

- 1) Significant and important revisions, such as :
 - Clearer and strong conceptual framework;
 - Clarified safeguard provisions and better connected to threats: it is understandable how PAs can handle the threats;
- 2) Enhanced Long Association (partner rotation) provisions;
- 3) Non-compliance with laws and regulations standards.

Renewed Code is a quite substantial contribution to the ability of PAs to work in the public interest and to keep and increase trust in the accountancy profession.

4.11 Revisions for clarification of the Applicability of Provisions in Part C of the Restructured Code to PAs in Public Practise

PAs in public practice (PAPPs) and PAs in business (PAIBs) can have similar problems and ethical dilemmas. In this reason based on the opinion of IESBA, the restructured Code should be clear regarding the matters in which the provisions in Part C of the new Code should also apply to PAPPs.

In the survey, members of IFAC have questions about the clarity of the statement "When facing an ethical issue, a PA shall consider the context within which the issue has occurred" in paragraph R120.4 of the Applicability ED. The part "...facing an ethical issue..." was not much clear to the respondents, because it meant that PA has already faced a specific ethics issue that should be addressed.

In restructured Code it was changed to "When dealing with ethics issue, the PA shall consider the context in which the issue has arisen or might arise". This change makes it clear that PA is responsible to consider an ethics issue irrespective of if it has already happened or not, and not to act proactively to address it.

The provisions in Part 2 of the new Code contains the matters mainly related to professional activities that happen internally within the employing entity, but there are some situations where those provisions will also refer to a PAPP when the PAPP provides professional services for clients or to the PAPP's client relationships.

IESBA mentioned, that the accent of the provisions on paragraphs R120.4, R300.5 and 300.5 A1 must with provisions in Part C of the extant Code, that is on individual PA.

The paragraphs R120.4 and R300.5 now state: "When dealing with an ethics issue, the professional accountant shall consider the context in which the issue has arisen or might arise. Where an individual who is a professional accountant in public practice is performing professional activities pursuant to the accountant's relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with the provisions in Part 2 that apply to these circumstances"⁶⁰.

Four examples were provided in paragraph R300.5 to illustrate a range of situations and problems where the provision in Part 2 could be applicable to PAPPs.

The conceptual framework laid out in Section 120 has bigger prominence in the reviewed Code and is important starting point for evaluating an ethics issue and determining how to address it in the best way. On that base IESBA proposed that the applicability paragraphs to be included in Part 1, Section 120, just after paragraph 120.3

⁶⁰ Handbook of the International Code of Ethics for Professional Accountants ____ including International Independence Standards. 2018

A1⁶¹. The proposed applicability paragraphs were repeated in Part 3, Section 300, right after paragraph R300.4 to reduce the risk of their being overlooked by PAPPs.

4.12 Improvement of the structure of the Code of Ethics for Professional Accountants

It is in public interest when the Code is written in usable and understandable manner. There was a feedback to the IESBA in the past, regarding the usability and clarity of the extant Code. For instance, small and medium practices (SMPs) have mentioned that the biggest barrier to follow the Code is in understanding its requirements. Some other shareholders indicated that they had issues with translating or understanding the long and complex sentences of the previous Code.

In 2014, the project to enhance the clarity and usability of the extant Code was approved by the IESBA.

As its December 2017 meeting, the IESBA approved the final text of the restructured Code with the affirmative votes of 16 out of 16 members present. The restructured Code includes⁶²:

- a) Structural and drafting enhancements developed under the Structure of the Code (Structure) project;
- b) Revisions to the provisions pertaining to safeguards in the Code, including enhancements to the conceptual framework, developed under the Safeguards project;
- c) Revisions to clarify the applicability to the provisions in Part C⁶³ of the extant Code to professional accountants in public practice (PAPPs), developed under the Applicability project⁶⁴, and

⁶¹ Paragraph 120.3 A1 contains application material outlining the content of each part of the Code and mentions that the conceptual framework is valid to all Pas.

⁶² Basis for conclusions prepared by the Staff of the IESBA, April 2018: Improving the Structure of the Code of Ethics for Professional Accountants

⁶³ Extant Part C – Professional Accountants in Business

⁶⁴ Part 1 – Complying with the Code, Fundamental Principles and Conceptual Framework, Section 120. The Conceptual Framework, paragraph R 120.4; and Part 3 – Professional Accountants in Public Practice, Section 300, Applying the Conceptual Framework – Professional Accountants in Public Practice, paragraph R 300.5 to 300.5 A1

- d) New application material relating to professional scepticism and professional judgment, developed under the Professional Scepticism (short – term) project.⁶⁵

4.12.1 Elements of restructuring

Main elements of restructuring contains the followings:

- a) Increasing the fame of the requirements to comply with the basic principles, be independent , if applicable, and use the conceptual framework;
- b) Stressing that compliance with the basic principles and, if applicable, be independent, are the main requirements of the Code;
- c) Differentiating requirements from application material;
- d) Increasing clarity of responsibility, particularly related to independence;
- e) Increasing the clarity of the language, improving readability and understandability; to make short and simpler sentences; to simplify complex and difficult grammatical structures and to avoid legalistic and archaic terms.

Furthermore, there some additional elements of restructuring:

- a) Improving the navigability of the Code, including adding a Guide to the Code;
- b) To organize the Code into more self-contained parts and subsections, so that:
 - Each Part has its own introduction to give an overview and content, including threats that could exist, and reminders of the requirement to comply with the basic principles, being independent, if applicable, and use the conceptual framework;
 - Improved numbering to clarify and facilitate future revisions.
- c) Reorganizing the Code to take advantage of forth coming electronic features;
- d) Improving the Glossary;
- e) Reorganizing the extent Parts B and C to identify the relevance of the material useful to PAIBs to PAPPs in concrete cases and so on.

Most definitions and descriptions has been put in the Glossary by the IESBA. The IESBA has added lists of abbreviations and standards referred to in the Code as well.

⁶⁵ Part 1, Section 120, paragraph 120.5 A1, 120.5 A 2 and 120.13 A1 to 120.13 A 2

Explanatory material has been added to "How to Use the Code" section of the *Guide to the Code*.

There is a new useful material in paragraphs 120.12 A1-120.12 A2 under the part named Considerations for Audits, Reviews and Other Assurance Engagements in Section 120:

- f) It provides with bigger prominence to meet requirement for PAPPs to be independent when providing audit and assurance services, and strengthens the connection between independence and the conceptual framework;
- g) It gives an explanation to the interaction between the independence sections and basic principles relating to the PA's responsibility to use the provisions in the conceptual framework to maintain independence. For providing an adequate context, the description of independence which is included in Parts 4A and B of the revised Code was repeated.

There are four self-contained Parts in the restructured Code. They are part 1,2,3 and the International independence Standards in Parts A and 4B. Each of the parts consists of different sections to address specific topics. The IESBA defined to add an overarching requirement to comply with the fundamental principles, be independent if applicable, and use the conceptual framework in Sections 200,300,400, and 900. It was made in purpose to overcome the risk that some PAs could not make needed link between the provisions in Parts 2,3,4 A and 4B of the renewed Code and those in the conceptual framework in Sections 120 in Part 1. Furthermore, they included the reference to the provisions in Section 120 in the introductory section of each Section of the restructured Code.

In the final parts of the restructured Code, limited revisions were made to the agreed-in-principle text to simplify the introductory paragraphs across the different sections in the Code and for bigger composition.

The IESBA has also reviewed the *Guide to the Code* to clarify how different parts of the restructured Code interact with each other and to stress PAs' responsibility to use the conceptual framework stated in Section 120.

Principle-based approach was retained in restructured Code.

The order of the requirements and application material in each section of the reviewed Code was reconfirmed to be as follows:

- General requirements and useful material on applying the conceptual framework are set forth first, and specific requirements follows them.
- Identifying the need for scalability, requirements that apply to firms when they provide professional services to public interest entities (PIEs) are set out after requirements that apply to other entities.
- Application material which is specific for a particular requirement follows the related requirement as tightly as possible.

The IESBA reaffirmed its view that the Code should refer to ISQC 1 and agreed to retain the following material in paragraph 400.4 of the restructured Code:

"ISQC⁶⁶ 1 requires a firm to establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, other subject to independence requirements, (including network firm personnel), maintain independence where required by relevant ethics requirements...Many of the provisions of this Part do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to "firm" for ease of reference..."

The IESBA also has done the followings:

- h) Defined the focus on addressing gap in the Code regarding the topics and problems that are situated in the Code instead of duplicating matters that are addressed in other authoritative literature;
- i) Agreed to maintain the new application material regarding the independence in Section 120 because it is supposed to refer to , but not copy the material in Section 400;
- j) Confirmed that all individual PAPPs and their firms are subject to the independence provisions in Parts 4A and 4B of the reviewed Code.

In many cases the terms like "network firm" and "firm" were not distinguished in the extant Code. Instead of this, it comprises both terms in one – "firm". The IESBA mentioned, that distinguishing those terms would give greater clarity to the Code.

⁶⁶ International Standard on Quality Control

The terms "may" and "might" were also distinguished. The IESBA agreed, that

- k) The word "may" should be used in the Code only in cases where PAs have specific permission to take a particular action, including as an exception to a requirement.
- l) The word "might" should be used to define the possibility of a matter arising, an event happening or an order of an action being taken.

The IESBA also added the terms "may" and "might" in the Glossary in the Phase 1 agreed-in-principle text.

The use of the phrase “generally” was reduced in renewed Code.

In the finalization of renewed Code, the IESBA reviewed with attention the provisions to make sure that there was maximum drafting consistency as possible. However, as with the extant Code, there are some examples, where provisions in Part 4A and Part 4B are different.

In restructuring the provisions in the extant Code, the IESBA has used a building blocks. The strengthened conceptual framework set forth in Part 1, Section 120, is valid for all PAs and is not repeated in the following Parts or sections. The IESBA did not make it as "step – by – step checklist", but it has a logical approach for PAs to recognize, assess, and address threats in every situation.

4.13 Comparison of the New Code of Ethics with the previous legal regulation

New Code of Ethics for Professional Accountants	Previous Code of Ethics for Professional Accountants
The name of the document: "International Code of Ethics for Professional Accountants (including International Independence Standards)"	The name of the document: "Code of Ethics for Professional Accountants"
2018 Edition (will be effective from June 15, 2019)	2016 Edition (was effective since July 15, 2017)
Parts of the Code are indicated by numbers: 1,2,3....	Parts of the Code are indicated by letters: A,B,C...
The first Part of the Code is about Complying with the Code, Fundamental Principles and Conceptual Framework	The first Part of the Code is about General application of the Code
The second part is about PAs in Business	The second part is about PAs in public practices
The third part is about PAs in public practices	The third part is about PAs in Business

Includes a Guide to the Code	Does not include a Guide to the Code
Has Glossary and Lists of Abbreviations	Does not have Glossary and Lists of Abbreviations
The term "network firm" is distinguished where appropriate	The term "firm" and "network firm" are not distinguished
The term "may" is more related to permission and the "might" is used to denote the possibility	The term "may" can denote both a permission and a possibility
The phrase was changed into : "When <u>dealing with ethics issue</u> , the PA shall consider the context in which the issue has <u>arisen</u> or <u>might arise</u> ".	The phrase "When facing an ethical issue, a PA shall consider the context within which the issue has occurred" is used in paragraph R120.4

Table 6. Comparison of the new and previous Codes of ethics for professional accountants.

Conclusion

The audit has an important role in the life of business entities. The auditor's main role is to check, inspect, learn and to give a confirmations regarding the financial statements and business records of the companies. They help to prevent and detect the frauds and errors.

In order to provide audit services, a licenced auditor should fulfil the particular requirements and have some professional and personal qualities.

In order to reach an economic success, capital providers and capital users should be confident in the financial health of the given business. In this matters auditors helps them by confirming that the given business has a correct data and reliable, or, the opposite, if there are some mistakes and frauds are detected.

There are many audit companies operating and providing audit services globally. Within them, so called Big four has a huge role. Consisting of the companies, such as Deloitte, PwC, EY and KPMG, they are famous for their high quality job and reliability. Big four companies have a very good reputation within shareholders and other people related to finance.

The company which was audited is higher valuated than the one which did not have an audit. If to compare the prices of the stocks of the company which was audited by some small local audit firm and the one, whose financial records were audited by the auditor from the Big four, the second company's value will be higher. The auditor with greater quality of his job and better reputation has a good value adding effect for the company.

While performing the audit services, it is important to follow the ethical standards. When auditors learn ethics, it helps them to better solve the issues, to better understand the right way, to realize if their opinion is right in the particular situation or not.

An auditor must be fully independent in his job and nobody or nothing should influence their opinion and conclusion. An auditor should try to avoid all of the threat that hi can face during his examination and preparation of reports.

The new regulatory document for auditors, the new International Code of Ethics for Professional Accountants was released by the IESBA in April, 2018 and will become effective from June 15, 2019. The Code sets the behavioral standard expected from professional accountant and it represents the recognition of profession of its public interest responsibility. The Code is also principle-based Code, and it is much more unforcable, fully restructured and contains many important revisions, clear destinction between the requirements and the application criteria and it gives much greated prominence on fundamental principles of ethics and independence. Restructured Code is much clearer, much easier to use and apply, and to translate. The includes considerable and substantial revisions, clearer and more robust conceptual framework, safeguards provisions clarified and better aligned to threats, strengthened Long association provisions.

The restructured Code is a very significant contribution to the ability of professional accountants to perform in the public interest and to keep and increase trust in the profession of accountants.

The Republic of Uzbekistan adopts its regulatory documents in accordance with International Accounting Standards and International Financial Reporting Standards. After the New International Code of Ethics will be effective from June 2019, the Ethical Standards for auditors in Uzbekistan will also change.

List of abbreviations

IEAASB - International Auditing and Assurance Standards Board

IFAC - The International Federation of Accountants

PA – Professional accountant

PAIB - Professional accountant in business

PAPP - Professional accountant in public practice

SMP – Small and Medium practices

IAASB - International Auditing and Assurance Standards BoardNAS

NAS - Non-assurance services

PIE – Public interest entity

ISA – International Standards on Auditing

SME - Small and medium sized entities

CPD – Continuing professional development

NOCLAR - Non-Compliance with Laws and Regulations

IPD – Initial professional development

ISQC - International Standard on Quality Control

ChAUz - The Chamber of Auditors

CPA - Certified Public Accountant

IFRS - International Financial Reporting Standards

CIPA - Certified International Professional Accountant

NAAA Uz - The National Association of Accountants and Auditors

PwC – PricewaterhouseCoopers

EY - Ernst & Young

KPMG - Klynveld Peat Marwick Goerdeler

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