

## Polish auditing norms and international standards on auditing

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### **Abstract**

The paper corrects errors in the description and interpretation of Polish statutory auditing in an article by Brody, Moscovice and Wnek (2005) called 'Auditing standards in Poland: past, present and future' published in the United States in the Managerial Auditing Journal. This critical review of the article is used as a basis on which to construct a more accurate view of the influence of International Standards on Auditing on Polish auditing norms. Nevertheless, these norms are found to contain specifically national features which differentiate the system of corporate governance in Poland from those in other EU member states.

“There is, indeed, some tenderness due to living writers when they attack none of those truths which are of importance to the happiness of mankind and have committed no other offence than that of betraying their own ignorance or dullness. I should think it cruelty to crush an insect who had provoked me only by buzzing in my ear, and would not willingly interrupt the dream of harmless stupidity or destroy the jest which makes its author laugh. Yet I am far from thinking this tenderness universally necessary. For he that writes may be considered as a kind of general challenger whom every one has a right to attack since he quits the common rank of life, steps forward beyond the lists, and offers his merit to the public judgment. To commence author is to claim praise, and no man can justly aspire to honour but at the hazard of disgrace.”

Samuel Johnson, The Rambler, No. 93, 5 February 1751.

## Introduction

This paper corrects errors, both of fact and of interpretation, concerning Polish statutory auditing contained in an article written by Brody, Moscovice and Wnek (2005) (hereafter: BMW, 2005) called 'Auditing standards in Poland: past, present and future' and published in the United States (US) in the Managerial Auditing Journal. A critical review of this article is used as a basis on which to construct a more accurate view of Polish statutory auditing reform and the current relationship between Polish auditing norms (PANs) and International Standards on Auditing (ISAs).

The statutory auditing issue is an important area of research because recent high profile corporate collapses have generated the political will in the European Union (EU) and internationally to improve the way in which companies are run and regulated. For example, an action plan has been developed to improve corporate governance and company law across the enlarged EU (European Commission, 2003). However, the enlarged Europe is a diverse entity in which traditions and practices in the area of corporate governance vary and so the question arises: which elements of good corporate governance practice at the national level should be adopted across the EU and why? Poland's corporate governance system in general and its statutory auditing element in particular has unique aspects which make it a particularly interesting field of study. Chief among these is the legal requirement to prepare and publish a long form audit report in addition to the usual short form report containing the audit opinion. This unique aspect renders an accurate depiction of the Polish statutory audit process an essential starting point in any research endeavour. However, recently published research in the English language academic literature on Polish

statutory auditing has not only failed to provide such a picture but has put into the public domain severely misleading characterisations of the Polish statutory auditing process. This paper corrects these errors and provides a much more accurate view of an extremely interesting, indeed unique, national framework for the statutory audit process.

The paper proceeds as follows. The next section presents a brief literature review which motivates the research. This is followed by a section which presents the regulatory background to the Polish statutory audit process in historical perspective. The next section is a critical review of BMW (2005) which corrects the article's errors in the context of a more accurate exposition of the Polish auditing process. The final section presents the conclusion to the paper and directions for future research.

### Literature review

The Polish corporate governance system has aspects which are unique – such as the preparation and publication of long form audit reports for listed entities – but which are little known and consequently under-researched. For example, a discussion paper written by the Brussels based Fédération des Experts Comptables Européens (FEE) on the financial reporting aspects of corporate governance recognised that the practice of statutory auditors providing expanded auditor commentary through long form audit reports existed in a minority of EU member states (FEE, 2003: 66):

In some countries a tradition has been built for detailed written communication, through either a management letter or a “long form” (extended and detailed) audit report.

However, at the time the discussion paper was prepared (which was prior to Poland's entry into the EU in 2004), FEE seemed unaware of the Polish situation with respect to the public availability of the long form audit report for listed entities, stating (FEE, 2003:66):

It is only distributed to the board and the audit committee and is not intended for audiences outside those charged with governance of the company.

This may be the case in Austria and Germany, but not in Poland. The Polish stock market regulator requires the publication of the long form audit report for all listed entities. This statutory auditing issue is important because research into expanded auditor commentary is currently being undertaken in the US by the American Institute of Certified Public Accountants (AICPA), which in a recently published report reinforced this commitment, stating that (AICPA, 2004: Chapter 7):

The Committee expects the AICPA Special Committee on Assurance Services to continue the process of research and exploration of auditor commentary.

It is vital that the practical experience in the EU with long form audit reports informs and influences this wider international debate. There have been calls in the United Kingdom (UK) for further research on the issue of expanded auditor commentary (or 'free-form reporting') (e.g. Hatherly, Brown and Innes, 1998; Hatherly, 2003) as well as UK Government interest in company law and corporate governance issues generally (DTI, 2005). Hence, research into the advantages and disadvantages of

nationally specific aspects of statutory auditing such as the expanded auditor commentary contained in Polish long form audit reports is both topical and necessary.

This research will provide useful input into some of the important issues that characterise the debates on corporate governance currently taking place in Europe and the US. For example, research work undertaken by the AICPA in the US reports that a "... majority of users support expanding auditor reporting to include some form of analytical commentary." (AICPA, 2004: Chapter 7). Users considered the views of the auditor to be valuable because they were perceived to be made from an independent perspective. Hatherly *et al.* (1998), on the basis of a sample of MBA students in a UK context, also report favourable user reactions to expanded auditor commentary. However, the AICPA research also identified a number of possible disadvantages such as: the possibly negative longer term impact on auditor independence and liability of providing such commentary; the impact on the content of the management's report of expanded auditor commentary; the costs of the new standards and skills involved.

As is evident from the FEE discussion paper (FEE, 2003:66), the continued lack of research in this area has resulted in misapprehensions as to the public availability of the long form audit report. Hence, an objective evaluation of its actual and potential role in the corporate governance of listed entities has been impeded. A small amount of descriptive research has been done on the content of Polish short form (Krzywda, Bailey and Schroeder, 1998) and long form audit reports (Schroeder, 1999) but the work is now out of date having been performed at a time when Poland was still very much in transition to a market economy and not a full member of the EU (the sample

of long form reports analysed related to the year ending 31 December 1996, for example).

More recent research on statutory auditing in Poland published in the English language has only served to complicate unnecessarily what is already a diverse area of European corporate governance and statutory audit practice. For example, with reference to the Polish situation, BMW (2005: 40) state:

The short-form audit report is to be made available to shareholders while the long-form audit report is submitted to the Polish treasury office as a tax regulation requirement only.

However, with respect to the long form audit report, the above statement is simply incorrect. As the sections below will show, the long form report is also required to be made available to shareholders prior to the annual general meeting but is not otherwise required to be made publicly available through, for example, filing or publication. The exception to this latter rule is the public availability of the long form audit reports of entities listed on the Warsaw Stock Exchange (WSE). Other errors concerning the Polish statutory auditing process to be found in BMW (2005) are dealt with below.

It is clear from this brief summary of the literature that little academic research has been done on this aspect of the Polish statutory auditing issue and that what has been done is now either out of date or simply inaccurate. One of the main tasks of this paper is to rectify this neglect.

### Regulatory background in historical context

The history of the audit of financial statements in modern day Poland begins in 1928. The statutory audit of financial statements was sanctioned by the Act on Joint Stock Companies 1928 which required the audit by expert auditors of the financial statements prepared by the founders of a joint stock company ‘... with regard to their truth and accuracy together with the aim of issuing an opinion as to whether the level of proposed remuneration was justified’ (Article 7). According to article 89, statutory auditors should audit annually the balance sheet, income statement and management report of a joint stock company. The statutory auditors were appointed by the registry court from a list put forward by the Chamber of Commerce. These regulations were later incorporated into the Commercial Code 1934. Both the Act on Joint Stock Companies 1928 and the Commercial Code 1934 which superseded it used the word ‘opinion’ [opinia] with reference to the short form audit report. However, the complex problem of the professional basis on which the work of expert auditors was conducted, including the specification of the detailed content of the opinion as well as the principles on which the audit profession should be regulated, did not find legal expression in the twenty year period between the two World Wars.

After 1945 and as a result of the transfer into state ownership of the majority of industry and trade the profession of statutory auditor lost its raison d’être. Towards the end of the 1950s, in conjunction with the reform of the system of state control, there was created an audit function with some of the attributes of the pre-war audit profession. A resolution of the Council of Ministers of 12 May 1959 on the matter of the financial audit of state-owned organisational entities introduced the title ‘state

authorised accountant' (SAA) whose task was charged with control functions not dissimilar to those exercised over joint stock companies by statutory auditors in the pre-war period. At the same time the obligatory annual audit of the financial statements was introduced. Also specified were the principles determining entry onto the official list of SAAs as well as the qualification requirements to be fulfilled by candidates to the new function. The regulations delegated the task of training and educating SAAs to the Association of Accountants in Poland (Stowarzyszenie Księgowych w Polsce - SKwP).

The detailed principles governing qualification as an SAA, the job function and the principles of auditing and approving financial statements were all regulated by orders, instructions and circulars issued by the state in the person of the Minister of Finance. SAAs initially audited financial statements on the basis of requests issued by the bodies which supervised state owned enterprises (e.g. industrial conglomerates) and later from the mid 1970s on the basis of requests from the tax authorities.

The end result of the audit of the financial statements as described above was a comprehensive (long form) report on the audit which was delivered to the body requesting the audit. This extensive document presented a detailed description and analysis of each item in the financial statements. This report on the audit was in turn verified by SAAs working on behalf of the body which requested the audit in the first place – the industrial conglomerate and later the tax office. These institutions had no motive to publish these reports on the audit and in any case the financial statements were of no interest to the other entities operating in the immediate environment of the audited entity.

The subsequent evolution of the Polish economic system towards a market economy required that the principles of auditing financial statements should be appropriate to the needs of such an economy taking into account the experiences of other market economies as well as using the knowledge gained hitherto, i.e. the qualifications and experience of the SAAs. In reviewing the audit opinions and reports issued by statutory auditors in a number of countries, attention was focused on the differing solutions adopted by the German and British systems. Taking into account Polish experiences in this area it was decided that the statutory auditor should be legally required to prepare a short form audit report, a separate long form audit report as well as supporting audit documentation. The delivery to the audited entity of a short form together with a long form audit report seemed to be a solution which contained within it the advantages of the British system (a short form audit report whose content is quickly communicated) and those of the German system (a long form audit report which can contain a greater quantity of useful information). The adopted solutions found expression in the Audit Act 1991 which also incorporated the knowledge and experience of the Polish SAAs.

In 1994 a new act on auditors and their self-regulation was promulgated (Audit Act 1994) while the regulations on the audit and publication of financial statements that were contained in the Audit Act 1991 were transferred into the Accounting Act 1994 which kept the requirement to produce a short form audit report, a long form audit report as well as the audit documentation. These new pieces of legislation were motivated by the need for Polish accounting and auditing reform to take into account EU directives.

The regulations with the highest authority over the statutory audit process in Poland are contained in the Accounting Act 1994, Chapter 7 of which is entitled ‘The audit and publication of financial statements’. In this chapter, Article 65(1) defines the purpose of the statutory audit, stating that (Puławska and Koziarkiewicz, 2005: 155):

The objective of an audit of the financial statements is a written auditor’s opinion and report on whether the financial statements are true, and give a fair and clear view of the financial position and the financial performance of the audited undertaking.

The important point in the quotation above is that there is a legal requirement for the Polish statutory auditor to produce at the end of the audit process not only a written short form audit report [opinia] but also a long form audit report [raport]. The contents of the short form and the long form audit reports as legally required by the Accounting Act 1994 are detailed in Tables 1 and 2 respectively.

In this same chapter of the Accounting Act 1994, Articles 68, 69 and 70 regulate the public availability of the audited annual financial statements, including the short form and long form audit reports. The public availability of the audited annual financial statements is regulated across three separate arenas: access by shareholders, filing as a matter of public record and publication in a nationally available official journal. Article 68 secures access for shareholders and requires that all financial statement data including the short form and long form audit reports be made available to shareholders not later than 15 days prior to the annual general meeting. Article 69 specifies the requirements for filing copies of the audited annual financial statements

after their approval by the annual general meeting of shareholders with the court register, where they become a document of public record and may be consulted by the general public. It is to be noted that while it is a requirement for the entity to file the short form audit report along with the audited annual financial statements with the court register, this requirement does not apply to the long form audit report which is therefore not a document of public record. Article 70 specifies the requirements for publication of the audited annual financial statements in abbreviated form in an official journal (Monitor Polski B) together with the short form audit report but, consistent with the legal filing requirements of Article 69, does not require publication in this nationally available journal of the long form audit report.

For the entities listed on the WSE, copies of the long form audit report are on file and a matter of public record at the offices of the securities market regulator and moreover are publicly available to be downloaded in electronic format from web portals such as <http://www.interia.pl>. Hence, uniquely in the context of corporate governance practice in the EU, the contents of the long form audit reports of Polish listed entities are publicly accessible. The requirement for listed entities to make the long form as well as the short form audit report publicly available has been obligatory from the very start of the functioning of the WSE in 1991. Current regulations require that listed entities send their annual and other interim financial statements, together with the short form and long form audit reports if applicable, electronically to the Polish Securities Commission (now superseded by the Financial Supervision Commission) which passes on the data to the WSE and to the National Information Agency (PAI – Państwowa Agencja Informacyjna) which in turn makes the data publicly available, e.g. on web sites. This brief overview of the legal framework of the Polish statutory

auditing process is supplemented by a more detailed commentary on the errors in BMW (2005).

#### Critical review of BMW (2005)

Early on in their article, BMW (2005: 38 – 40) present a brief history of Polish accounting and auditing but one which is both confused and confusing. For example, BMW (2005: 39) state:

In 1957, the Institution of Audit Experts was established in Poland to verify accounts of state-owned enterprises with the appointment of State Authorized Accountants (SAA).

In fact, there was no separate institution so named. SAAs formed part and parcel of the membership of the SKwP although, considered as something of an elite due to the very demanding examinations which they had to pass to obtain the SAA qualification, they did have a separate committee within the SKwP called the Krajowa Rada Dyplomowanych Biegłych Księgowych [National Council of State Authorised Accountants]. The term SAA is generally taken to have been officially introduced into Polish terminology by a decree of the Council of Ministers dated 1959 and not 1957 as stated by BMW (2005) (Bień, 2007:80).

However, later on in the article, in a section headed ‘The audit profession’, BMW (2005: 41) rather confusingly go on to state:

In 1960, the Ministry of Finance in Poland introduced the chartered accountant designation. Prior to the reforms in Poland, chartered accountants tended to hold managerial positions in accounting departments of enterprises. To obtain the chartered accountant's designation, individuals had to pass examinations in accounting, commercial law, and controls. The chartered accountants examined and issued certificates of correctness of enterprises' financial statements on behalf of the Finance Ministry during a special three-week release from their own place of work.

Initially, as the reader tackles this paragraph, he or she is entitled to conclude that the 'chartered accountant' designation referred to above is a completely different animal from the SAA qualification mentioned previously. If the paragraph above is taken at face value, the reader is forced to conclude that, prior to 1989, Poland had two sets of specialists verifying the financial statements of state-owned enterprises: SAAs (established in 1957) and chartered accountants (established in 1960). In truth, however, there was but one auditor qualification in the Polish command economy, the dyplomowany biegły księgowy, usually translated as 'state authorised accountant'. There is no separate 'chartered accountant' designation as such and judging from the quotation above BMW (2005) may have mistaken two different translations of the same Polish phrase as an indication of the existence of two separate audit qualifications. Alternatively, the authors may have had in mind the improvement that occurred in 1960 with respect to the status of the chief accountant (główny księgowy) of a state-owned enterprise. The chief accountant's rank within the organisation was increased to one level with that of Deputy Director and the chief accountant's work was re-graded from an administrative grade to the higher technical and economic grade (equivalent to planners) as a result of an increase in the scope of the chief accountant's duties to include internal financial control and the prevention of the wastage of resources by the enterprise (Bień, 2007: 81-82). Either way and however

explained, this sort of error is unlikely to result in an accurate understanding of the evolution of the Polish audit profession.

BMW (2005: 40) state:

Additionally, Audit Act 2000 [sic] regulated operation of the National Chamber of Statutory Auditors (NCSA).

For the avoidance of doubt, the NCSA (Krajowa Izba Biegłych Rewidentów – KibR) came into existence in 1992 as a result of the provisions of the Audit Act 1991 and is currently regulated by the Audit Act 1994, as amended in 2000. BMW (2005: 41) state:

In 1992, chartered accountants became certified public accountants (CPAs).

In fact, SAAs who qualified as such under the previous command economy rules were entitled to become members of the KibR which was formally established in 1992 as an organisation representing statutory auditors separate from but (at least initially) dependent financially on the SKwP.

Currently, a qualified Polish statutory auditor is known as a biegły rewident and the law guarantees the statutory audit profession exclusive use of this designation. As at the beginning of 2007, according to data available on the KibR web site, about two thirds of all 1,900 entities listed as being entitled to audit financial statements were

sole practitioners, while the vast majority of the remainder were incorporated as limited liability companies (Sp. z o.o.) but with a majority of statutory auditors on the management boards (although beneficial ownership as opposed to control could lie elsewhere with persons who were not statutory auditors). Given that the audit function under the command economy was undertaken on a part time basis at rates of pay determined by the state, it is far from surprising that the individual members of the indigenous audit profession, previously SAAs, have lacked the risk capital to compete on a level playing field with multinational audit firms in the new market for statutory audit services at the beginning of the transition process. The decision of the SKwP to invest its own capital in the creation of specifically Polish owned and managed audit firms in major commercial centres across the country was an acknowledgement that only a few individuals could surmount the considerable risks involved in setting up one's own audit firm in a transitional economy. The KibR is no longer subsidised by the SKwP, however, generating (according to its 2005 financial statements) revenues from the supervision of its members' provision of professional services (54 per cent), examination fees (22 per cent) and individual membership subscriptions (12 per cent).

Early on in their article, BMW (2005: 37) state that:

Poland began the process of negotiating entry to the EU in the spring of 1998.

This rather bald statement of fact is technically correct: at the Luxembourg summit in December 1997, the then existing 15 member states of the EU decided to open formal accession negotiations with the group of so-called 'Luxembourg countries' which included Poland (along with Croatia, Estonia, Hungary, Slovenia and Cyprus) on 31

March 1998. However, this date is very far from marking the start of an accession process that began much earlier. For example, the EU had signed a 'Europe Agreement' with Poland as early as 1991 and Poland's application for EU membership had been submitted in April 1994, shortly after the June 1993 Copenhagen summit at which the EU member states adopted an enlargement strategy which effectively encouraged applications for membership from the transition economies of the former Soviet bloc. Formal accession negotiations were completed at the Copenhagen summit in December 2002; the accession treaty was signed in April 2003 and Poland acceded to membership one year later.

Putting the sequence of events in the EU accession process in correct chronological order is important in understanding the progress of accounting and auditing reform in transition Poland. For example, BMW (2005: 37) state:

The first phase of this [accession] process involved identifying differences in the legal systems of the EU and Poland so that these differences could be eliminated. The end objective of the process was the adapting of Polish law to be consistent with the EU legislative heritage (i.e. acquis communautaire [sic] – a package of regulations that describe the functioning of a uniform market).

These comments are correct in principle but their appearance after the statement that accession negotiations began in 1998 creates the misleading impression that in practice accounting and auditing reform based on the EU model did not begin in earnest until after this date. In fact, reform in Poland began much earlier, as BMW (2005: 39) themselves acknowledge albeit without perceiving the inconsistency with the timescale implied in their previous statement:

The key phase of the formation of Polish auditing standards started in January 1995 with the introduction of a new legal act driven by the incentive of fast accession to the EU.

The ‘new legal act’ referred to in the above quotation was the Audit Act 1994 which, together with the Accounting Act 1994, incorporated key elements of the EC’s Fourth, Seventh and Eighth Company Law Directives into Polish parliamentary legislation to render accounting and auditing regulations largely consistent with the acquis communautaire. For both accounting and auditing, therefore, broad consistency with the acquis had been achieved several years before the opening of formal accession negotiations in 1998.

The misinterpretation of the historical sequence of events in BMW (2005) may be the cause of the factual errors which appear later on in their article. For example, BMW (2005: 39) incorrectly state:

In September 2000, the new Audit Act (Ustawa z dnia 21 wrzesnia o bieglych rewidentach) [sic] was issued.

If the start of the process of EU accession is taken to be 1998 (albeit incorrectly) it is perhaps understandable that what is in fact merely a revision to the earlier Audit Act 1994 should be incorrectly interpreted as a completely new piece of parliamentary legislation initiated in order to ensure compliance with EU laws. Further on in the article (BMW, 2005: 40) the authors again refer to the ‘Audit Act of September 2000’ and the ‘Audit Act 2000’. Revealingly, there is no reference to this act in the article’s

bibliography (BMW, 2005: 46). What BMW (2005) seem to present as a new act is in fact a revision to the original Audit Act 1994 dated 2000 and prompted by several years of practical experience in implementing and enforcing the original 1994 legislation.

The existence of an 'Audit Act 2000' is also incorrectly assumed by Kosmala MacLulich and Sucher (2004: 68):

The Audit Act 1994 was superseded by amendments brought in by the Audit Act of 2000 (Audit Act 2000), applied from November 2000.

This sentence is inaccurate and based upon a misunderstanding. The full name of the act promulgated in 2000 and referred to in the above quotation was actually the Ustawa o zmianie ustawy o biegłych rewidentach i ich samorządzie (Dziennik Ustaw, 2000, No. 89, item 992) which translates as 'Act on changes to the act on statutory auditors and their self-regulation'. A similar error is made by Leško (2007: 62):

In September 2000, the Audit Act of 1994 was also superseded by a new Audit Act (*Ustawa z dnia 21 września, 2000*).

The original Audit Act 1994 has not been superseded but merely amended by the provisions of the act dated 2000. An existing act of parliament can only be amended by legislation of equal (or superior) rank or authority. This is why, on the web site of the KibR the available text of the legislation is that of the Audit Act 1994 in its

uniform and consolidated version of the text as published in the Dziennik Ustaw in 2001.

Kosmala MacLulich and Sucher (2004: 67) make a similar error with respect to accounting regulations and mislead the reader into believing in the existence of an Accounting Act 2000 which superseded the Accounting Act 1994 rather than simply stating that in November 2000 the Polish parliament passed the Ustawa o zmianie ustawy o rachunkowości (the Act on changes to the act on accounting) (Dziennik Ustaw, 2000, No. 113, item 1186). The provisions in the 2000 act cannot be understood without reference to the original articles in the Accounting Act 1994 that they are amending and, as in the case of the Audit Act 1994, required the publication of a uniform and consolidated version of the text of the original Accounting Act 1994 (in 2002). Leśko (2007: 61) is more accurate in his description of the changes in Polish parliamentary legislation on accounting, but his suggested approach to dealing with the designation of the act can hardly be condoned:

On 9<sup>th</sup> October 2000, the Act on Accounting of 1994 was amended (*Ustawa z dnia 9 listopada, 2000*) in order to achieve greater compliance with both the EU regulations and IAS. The amended Act on Accounting of 1994 (for clarity's sake further referred to as the Act on Accounting of 2000) ....

Leśko's suggestion for re-naming, far from achieving clarity, would make it impossible for a reader to distinguish between acts of parliament that have been repealed and replaced and those which have been merely subject to minor amendments.

An understanding of the genesis of the Audit Act 1994 is an important element in appreciating the nature of the legislative framework which governs Polish statutory auditing in general. BMW (2005: 39) state:

The new parliamentary act, Ustawa z dnia 29 października 1994r. o bieglych rewidentach I ich samorzadzie [sic] (i.e. the Statutory Auditors and their Self Regulation Act 1994), superseded and expanded the auditing regulations contained in the Audit Act 1991.

While ‘superseded’ is a correct interpretation of the effect of the new 1994 act, ‘expanded’ is not, as Table 3 makes clear. The provisions in the Audit Act 1991 which regulated the obligatory annual audit of financial statements (i.e. what work is to be done and how it is to be reported) were transferred to the Accounting Act 1994 hence reducing (not expanding) the scope of the Audit Act 1994 to those provisions regulating the audit profession (i.e. who is qualified to do the audit work). The regulatory framework of statutory auditing in Poland has two legislative sources of equal weight and importance, the Accounting Act 1994 and the Audit Act 1994, regulating distinct aspects of the statutory audit function as defined by the introductory article to each act reproduced in Table 3.

With reference to the period covered by the legislative developments depicted in Table 3 (1991 – 1994), BMW (2005: 39) state:

These years in particular were influenced by the mass privatization of state-owned enterprises and an on-going harmonization process within the provisions of European law.

While it is difficult to imagine an ‘on-going harmonization process’ taking place out-with the ‘provisions of European law’, the influence of the mass privatisation programme at this juncture (1991 – 1994) is overstated by the authors. Politically controversial from the very outset, mass privatisation legislation did not reach the statute book until mid 1993 and the privatisation of several hundred companies via national investment funds was still only in plan form as late as October 1994. One of the most important real influences on the reform of Polish statutory auditing during this early transitional period was the newly established state regulator, the Securities Commission in charge of the fledgling and recently re-established WSE. The initial privatisation strategy was to sell leading state-owned enterprises not by mass privatisation but by public share offerings which required the close cooperation of the foreign multinational audit and consultancy firms (providing market economy expertise not available indigenously) and the stock market regulator in the form of the Polish Securities Commission. The alliance between these two new players in the Polish transitional economy had a material impact on the promulgation of the Audit Act 1991. For example, the chairman of the Securities Commission spoke in favour of the Audit Act 1991 in the Sejm, the lower house of the Polish parliament, asserting the paramount importance of the annual statutory audit for the future development of a credible securities market. From the point of view of the multinational audit firms, the Audit Act 1991 created a market for their statutory audit services by enshrining in modern day Polish law the obligation for all entities of any substantial size to have an annual audit. Crucially, the statutory auditor was to be chosen by the entity to a term of office which lasted from one annual general meeting to the next. The command economy system of SAAs appointed to the statutory audit by the tax office was

effectively superseded in favour of a market economy system in which the multinational audit firms could compete on what was to them familiar ground.

To what they call the ‘comprehensive amendments’ to the Accounting Act 1994 enacted in 2000, BMW (2005: 40) attribute incorrectly the fact that:

The accounting regulations have moved the focus of Polish accounting away from an emphasis on tax compliance toward a more business-oriented approach, directed at meeting the information needs of various stakeholders in a Polish market economy.

In fact, the distinction between accounting profit and taxable profit was first established in the Accounting Act 1994; the amendments in 2000 brought Polish legislation generally more into line with updated IFRS and IAS and for deferred taxation in particular with IAS 12 Income Taxes (which was in a revised version effective from 1 January 1998). The point is that the original Accounting Act 1994 contained provisions which regulated how to account for deferred taxation – the latter concept simply did not arise in the earlier Accounting Decree 1991 because all timing differences between accounting and taxable profit were permanent. However, the Accounting Act 1994 which superseded the 1991 legislation from 1 January 1995 left to the discretion of the individual entity as a matter of accounting policy choice the option of continuing to use tax depreciation rates to determine accounting profit. The de facto impact of this change in emphasis is probably less extensive than suggested in the article, therefore.

The authors continue (BMW, 2005: 40):

The Audit Act 2000 [sic] introduced standard wording for the short-form and long-form formats of audit reports due to the differences between the legally required contents of these reports.

Although the act referred to in the above quotation is non-existent, it is nevertheless true that there are differences between the legally required contents of the two audit reports mentioned but these are to be found in the Accounting Act 1994, in Chapter 7 (Articles 64 – 70). However, there is nothing in this chapter or indeed anywhere else in the act that can even remotely be considered as introducing ‘standard wording’ for either of the audit reports. The first part of the quotation above is simply incorrect. However, in this case the authors are sufficiently attuned to the rather unfamiliar surroundings in which they find themselves to find it necessary to attempt some sort of an explanation for the rather unusual circumstance of having to deal with the existence of two audit reports rather than just the usual one. BMW (2005: 40) continue:

A short-form audit report provides a written opinion on the correctness and truth of an enterprise’s financial statements, including the date and place of their preparation.

The article does not make clear why the authors consider that an auditor’s written opinion should be required on, of all things, the date and place of the preparation of the financial statements. These would be, in the normal sense of the term, matters of fact and not of opinion but the authors let pass this rather unusual circumstance in

auditing terms without any comment or explanation whatsoever. This paper considers that the comment is a misunderstanding on the part of the authors and confirms that there is no such audit requirement in the Polish legislation.

The purpose and contents of the short form audit report are specified in Articles 65(1) to 65(4) of the Accounting Act 1994 and these are reproduced in Table 1. The legally required contents are found to be much more detailed and extensive than specified by BMW (2005: 40). There is no explicit mention of ‘standard wording’ in the Accounting Act 1994 although it is only to be expected that the terminology of the act will find expression in the wording of the audit opinion itself for obvious reasons. The Polish legal requirements as regards the content of the short form audit report demand nothing unusual of the auditor compared to other national and international norms. The one exception (not mentioned by BMW (2005)) might be the requirement contained in article 65(3) (1) in which the statutory auditor is obliged to mention the fact in the short form audit report should the entity have failed to file or publish in accordance with the requirements of the act any financial statements relating to previous years. This requirement needs to be seen in the context of Poland’s command economy history in which it was not standard practice to make the financial statements of enterprises publicly available. As a consequence of this reporting requirement, the statutory audit firm effectively becomes a state-appointed monitor of the transparency of its client’s business affairs, which role may be especially important in the prevention and detection of commercial abuses during a prolonged transition to a market economy. Recent concerns in the UK and elsewhere concerning the takeover activities of private equity firms illustrate the nature of this transparency problem.

BMW (2005: 40) then turn their attention to the second audit report required by Polish legislation:

A long-form report contains a statement that the enterprise's financial statements were prepared in accordance with the law and generally accepted accounting principles (GAAP).

In fact, the statement that the enterprise's financial statements were prepared in accordance with the law is required to be made in the short form and not the long form audit report (Table 1, art. 65(2)). Additionally, there is no legal requirement for the auditor to state anything at all in respect of GAAP in the Polish context. In characterising the contents of the long form audit report as they do in the quotation above, BMW (2005) are simply incorrect. The errors in respect of the contents of the long form audit report continue, however (BMW, 2005: 40):

The latter report also includes an opinion on the correctness and truth of the enterprise's financial statements with the specification that data [sic], which in comparison with the previous accounting period, indicated circumstances which materially and negatively impacted on operating results and the financial situation of the reporting entity.

As Table 2 makes clear, the legally required contents of the long form audit report are very different from and much more extensive than the characterisation above. BMW (2005) fail to state why the opinion on the correctness and truth of the enterprise's financial statements is duplicated in the long form report resulting in the disturbing implication that the two opinions – the other contained in the short form audit report -

may somehow differ. The second half of the quotation above is difficult to understand, perhaps due to one or more typographical errors in the text. However, it reads like a poorly understood version of the reporting requirement contained in Article 65(5) (7) of Table 2. It is to be noted that any serious going concern threats are to be reported in the short form audit report in any case (Table 1, Art. 65(3) (2)). Comparing the description of the contents of the short form and the long form audit reports provided by BMW (2005: 40) with those actually required by legislation and detailed in Tables 1 and 2, it is clear that BMW (2005) have not done justice to the sophistication and comprehensiveness of Polish legislation in the area of audit reports. Unsurprisingly, they have failed to appreciate the unique nature of the system they are (inaccurately) describing.

However, the errors in the description of the contents of the two audit reports are exacerbated by further errors with regard to the specification of their public availability – which characteristic is used by BMW (2005: 40) to distinguish between their required contents:

These differences in the contents of the audit reports are dictated by their public availability. The short-form audit report is to be made available to shareholders while the long-form audit report is submitted to the Polish treasury office as a tax regulation only.

The implication that only tax officials will see the long form audit report sits uneasily with the conclusion expressed only a moment ago by the authors in the article's previous paragraph that the focus of Polish accounting had moved away from an emphasis on tax compliance. If the analysis of the content of the long form audit

report provided by BMW (2005: 40) is taken at face value, the reader is forced to accept the frankly ludicrous notion that only tax officials (and no one else) is entitled to know if the entity's financial statements were prepared in accordance with the law and GAAP and only they are entitled to be informed of any circumstances which impact materially and negatively on the financial situation of the reporting entity because these are statements which, according to BMW (2005: 40), are contained in the long form audit report with its tax restricted availability. The idea that such important outcomes of the audit process should be made available only to the tax authorities is a notion of such inherent implausibility in statutory auditing terms that its serious academic expression can only be attributed to non-rational, cultural factors.

The actual reporting requirements to the tax authorities, who have a perfectly legitimate interest in the products of the audit process in a transition or a market economy, are specified in the Income Tax Act 1992 (Article 27(2)):

Taxpayers obliged to prepare financial statements are required to send them to the tax office together with the short form and long form audit reports of the entity entitled to audit the financial statements not later than 10 days after their approval at the annual general meeting; for companies, a copy of the resolution approving the financial statements is also required.

Unsurprisingly, the tax authorities require the full package of financial information produced by the entity and are unlikely to be satisfied with just a copy of the long form audit report and nothing else. However, the long form audit report is also required to be made available to the shareholders, as specified by the Accounting Act

1994 and so the statement in BMW (2005: 40) that the long form audit report goes to the tax authorities only is incorrect.

While it is correct to say that there is a difference between the short form and the long form audit reports with regard to their public availability, the difference is not correctly specified by BMW (2005: 40). The short form audit report is a document of public record which together with the audited financial statements is on file at the entity's local registry court and published in a nationally available government periodical (Monitor Polski B, the 'B' series having been specially created for the sole purpose of publishing financial statements and short form audit reports). The long form audit report has a more restricted circulation but exceptionally for listed companies on the WSE is made publicly available.

BMW (2005: 40) conclude this brief review of the products of the audit process as follows:

In summary, under the present Polish regulation framework, audit opinions are required to state whether the accounts of the enterprise present a true and fair view on the basis of correctly maintained accounting records and comply with law and accounting regulations.

The phrase 'true and fair view' cited above is used much too loosely by the authors and, arguably, only has any meaning in its native UK context in any case. The Polish written opinion is (first) on whether the financial statements are correct [prawidłowe] and (secondly) on whether they faithfully [rzetelnie] and clearly [jasno] present the asset and financial situation and financial result of the audited entity. The Polish wording is longer and more complex than the short paraphrase 'true and fair view'

implies. The translation into English of the uniform text of the Accounting Act 1994 which is available on the Polish Ministry of Finance web site has the following rendition of the relevant article (65(1)):

An audit of financial statements is aimed at expressing by a statutory auditor [sic] a written opinion together with a report on whether the financial statements are correct, and give a true and fair presentation of the property and financial position and the financial result of the audited entity.

Insights into the possible meaning of these phrases have been provided by Kosmala MacLulich (2003).

More errors occur in BMW (2005: 41) concerning the relationship between what they term the ‘Accounting Act of 1994’ and entities listed on the WSE. For example, it is incorrect to state that the Accounting Act 1994 requires listed entities to have a review by an independent statutory auditor of their half-year financial statements undertaken and published – this is actually a requirement imposed by the securities market regulator. Additionally, BMW (2005: 41) state:

Moreover, between 2001 and 2002, these companies were required to include in their financial statements a description of major differences between their adopted accounting policies and international accounting standards requirements.

Again, this requirement is not in the Accounting Act 1994 but in legislation promoted by the securities market regulator and the requirement in fact extended into 2003 while in 2004 a numerical reconciliation was required between profit and net asset

figures under Polish requirements as specified in the Accounting Act 1994 and international financial reporting standards (Krzywda and Schroeder, 2007).

Later on in their article, BMW (2005: 43) address the topic of the PANs issued by the KibR and list eight auditing standards. However, given that their article was published at the beginning of 2005, it is strange that the authors should list as current those PANs which had been superseded by resolutions of the KibR dating as far back as November 2002. The replacement of the eight old standards with the revised standards listed in Table 4 was effective for the statutory audits of all financial statements beginning 1 January 2002 or later. As a result, the deficiencies of PANs identified by BMW (2005: 44-45) with respect to ISAs are very much out of date. In Table 5 are referenced those ISAs that are covered in the revised PANs. The majority of the ISAs which BMW (2005: 45) claimed were not covered by PANs are now seen to be included in PAN No. 1. Tables 4 and 5 present a much more accurate and up to date picture of the relationship between ISAs and PANs.

The different approach of the Polish auditing profession to the question of setting auditing norms needs to be noted. With reference to the eight old PANs, the issuance of auditing norms tailored according to the nature of the business of the entity (insurer, bank or other) represents, in one sense, a throwback to the previous command economy tradition in which SAAs were qualified to audit not generally but in a specific branch industry and no other. The new PANs (Table 4) exhibit less evidence of this approach but continue to adopt a strategy which involves the issue of a smaller number of much more comprehensive auditing norms.

## Conclusion

The paper critically reviews recently published research in the English language on the Polish statutory auditing process and finds it seriously deficient. A much more accurate and up to date picture is presented instead which highlights the unique nature of some aspects of the Polish corporate governance and statutory auditing processes. The uniqueness of the Polish approach is a once a strength and a weakness in that on the one hand its inherent interest from a research point of view is balanced on the other hand by its inability to produce results of general applicability. However, future research is planned on the actual content of long form audit reports which, together with data from interviews with Polish statutory auditors, will provide more relevant results on the more general audit research issue of expanded statutory auditor reporting.

**Table 1: Legally required contents of the statutory auditor's short form report as specified in Article 65 (2-5) of the Accounting Act 1994**

Ref.	Detail
65(2)	<p>The opinion, referred to in paragraph 1, should, in particular, state whether the audited financial statements:</p> <ol style="list-style-type: none"> <li>1) have been prepared on the basis of properly kept account books,</li> <li>2) have been prepared in accordance with the accounting principles laid down in this Act,</li> <li>3) their form and contents comply with the applicable laws, statute or company deed,</li> <li>4) give a fair and clear view of all information relevant to the appraisal of an undertaking, and with regard to the management report, whether the information contained therein takes account of the provisions of article 49.2 and is consistent with the information included in the annual financial statements.</li> </ol>
65(3)	<p>The opinion should also:</p> <ol style="list-style-type: none"> <li>1) provide information on non-fulfilment, as at the date of the auditor's opinion, of the obligations laid down in Articles 69 and 70 of this Act, to file with a relevant court register and publish the financial statements for one or more years preceding the financial year,</li> <li>2) indicate any serious threats to the undertaking's continuing as a going concern detected during the audit.</li> </ol>
65(4)	<p>The opinion should explicitly identify the reasons for expressing a qualified opinion on the financial statements, an adverse opinion or a refusal to give a [sic] an opinion due to the circumstances which prevent its formulation. Qualifications should be expressed in a manner which indicates their extent.</p>

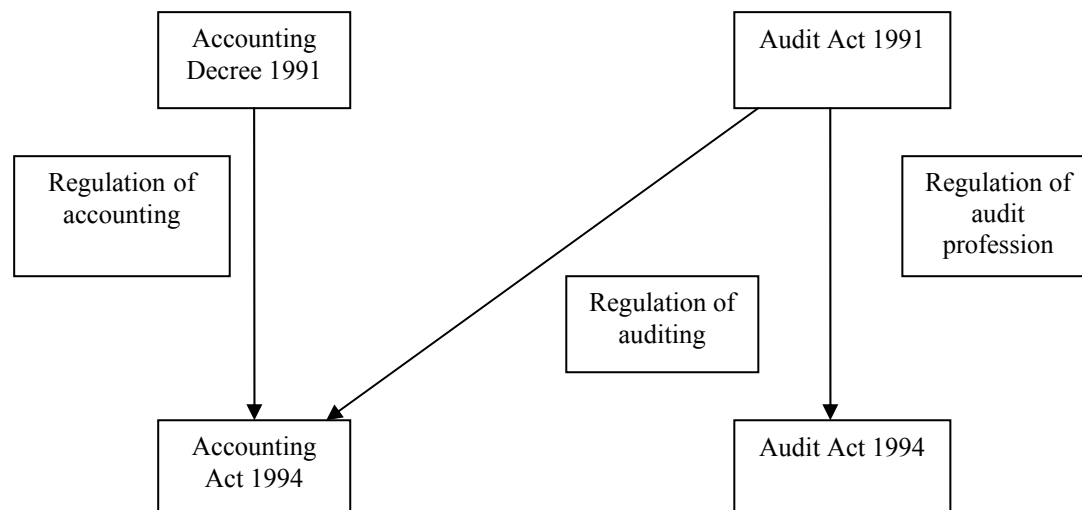
Source: Puławska and Kozierekiewicz (2005: 155).

**Table 2: Legally required contents of the statutory auditor's long form audit report as specified in Article 65 (5) of the Accounting Act 1994**

Ref.	Detail
65(5)	<p>The report, referred to in paragraph 1, should present, in particular:</p> <ol style="list-style-type: none"> <li>1) a general description of an undertaking (identification data),</li> <li>2) a statement that required information, clarifications and declarations have been received from an undertaking,</li> <li>3) an evaluation of the correctness of the accounting system applied,</li> <li>4) a description of the financial statements items or groups of items, if in the auditor's opinion they need to be discussed,</li> <li>5) a statement that a bank complies with prudential requirements, laid down in separate regulations, as well as a statement that the solvency ratio has been correctly determined,</li> <li>6) a statement that an insurance company has established technical reserves in the amount guaranteeing satisfaction of all current and future liabilities under insurance contracts, and that those reserves have been matched by investments, in accordance with the insurance regulations, as well as that the solvency margin has been calculated correctly and there are sufficient funds to cover that margin,</li> <li>7) a presentation of an undertaking's property and financial position, as well as its financial result, indicating the developments which, as compared with previous reporting periods, have a significant adverse effect on that position, in particular jeopardize the continuing of activities by an undertaking as a going concern. If in the course of an audit an auditor finds out that the law, statute or company deed have been seriously violated and such violation has an effect on the financial statements, such information should be included in the report and, if necessary, also in the opinion.</li> </ol>

Source: Puławska and Koziarkiewicz (2005: 155-157).

**Table 3: Accounting and Auditing reform in Poland: Early Legislative Developments**



<b>Accounting Act 1994</b>		<b>Audit Act 1994</b>	
Art. 1	This act specifies the principles of accounting and the procedures for the audit of financial statements by statutory auditors.	Art. 1(1)	This act specifies the principles for practising the statutory audit profession and the structure of the self-regulatory body of statutory auditors.

**Table 4: Auditing standards issued by the KibR in force as at 31 December 2005 (including guidelines)**

No.	Title
1	General principles of auditing financial statements
2	Specific principles of auditing the financial statements of entities in the financial sector
3	The audit of consolidated financial statements
4	General principles for the performance of a review of the financial statements
5	The principles to be followed by entities entitled to audit financial statements in the matter of the audit of financial statements and other verification services undertaken by statutory auditors
<p>Guidelines on the matter of preparing an opinion on the audit of the financial statements</p> <p>Guidelines on the matter of preparing a report on the audit of the financial statements</p> <p>Guidelines on the matter of the participation of the statutory auditor in the physical stocktaking</p>	

Source: Krzywda (2005: 46).

**Table 5: A Comparison between the Contents of Polish Auditing Norm (PAN) No. 1 and International Standards on Auditing (ISAs)**

<b>PAN No. 1 General Principles of Auditing Financial Statements</b>		<b>ISA No.</b>
<b>Chapter</b>	<b>Headings</b>	
I	General provisions	
II	The aim of the audit of the financial statements	
III	Audit methods	401,530
IV	Audit evidence	
V	Audit planning	
	Specific audit problems	
	Financial statements audited for the first time	510
	Participation in stocktaking	
	The audit of contingent liabilities and claims	
VI	The audit of estimated data	540
	Comparatives	710
	Post balance sheet events	
	Going concern	
	Management report	720
	Small entities	
	Related party transactions	550
VII	Abuses, errors, infringements of the law	240
VIII	Using the work of other auditors, internal auditors and experts	610,620
IX	Short and long form audit reports – common provisions	
X	Short form audit report	
XI	Long form audit report	
XII	Audit documentation	
XIII	Concluding provisions	

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