Term Project

China: Accounting Profession, Standards, and Future

~~Chinese Accounting Standards~~

Prepared by

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Was PowerPoint forwarded to me?

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Form OK but writing style issues, e.g., pagination, etc. Substance overall incomplete. There should be 20 pages of text without tables, figures, graphs, etc. Most recent reference is before 2014.

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Objective omitted! OMITTED Organization omitted

I. Introduction

The International Financial Reporting Standards (IFRS) are a set of accounting standards developed by the International Accounting Standards Board (IASB) which are used approximately in 120 nations and reporting jurisdictions. Significant differences exist between IFRS and U.S. Generally Accepted Accounting Principles (GAAP). IFRS is considered more of a "principles based" accounting standard in contrast to U.S. GAAP which is considered more "rules based." By being more "principles based", IFRS, arguably, represents and captures the economics of a transaction better than U.S. GAAP.

Not an Introduction

The Chinese accounting standard systems is composed of Basic Standard, 38 specific standards and application guidance. 2 sentences per ¶

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Chinese accounting standards are unique because they originated in a socialist period in which the state was the sole owner of industry. Therefore, unlike Western accounting standards, they were less a tool of profit and loss, but an inventory of assets available to a company. In contrast to a Western balance sheet, Chinese accounting standards did not include an accounting of the debts that a corporation holds, and were less suitable for management control than for accounting for tax purposes.

This system of accounting was widely considered to be unsuitable for managing corporations in a market economy. In 2006, the Chinese government introduced a revised accounting law. This was the fruit of considerable discussion and protracted debate, involving the Ministry of Finance, members of the International Accounting Standards Board (IASB) and representatives of some Chinese firms.

This revised law marked a large step forward for the continuing integration of world trade and capital markets, with China adopting a significant number of the accounting standards laid out by

Not an Introduc

the International Accounting Standards Board. The old Chinese Accounting Standards (CAS) were largely replaced by the International Financial Reporting Standards (IFRS), to bring China more in line with the rest of the world. The similarity between the new Chinese accounting standards and the IFRS is almost 90–95%. (Citation)

out of place

II. History of Chinese Accounting Standards

The W? western accounting system was first adopted in 1912 by the government-owned Bank of China. By 1916, the country's entire accounting system has been converted to the new system, replacing the traditional Chinese system. This policy was soon followed by other banks in the country. By the 1930s the western accounting system has been adopted by all government agencies, government-owned enterprises and modern financial institutions. However, the direct use of the debit-credit system in non-government business sectors met resistance, because the recording symbols, the forms of accounts, the Hindu-Arabic numerals and indeed the entire framework we so different.

The accounting development in China between 1949 and 1978, as in the case of its political and economic development, was under the influence of the Soviet Union, although there were certain unique features reflecting the political and economic conditions in China. The debit-credit accounting method which was widely used by government organs and modern business firms prior 1949 continued to be used as this was also the method used by the Soviet Union.

After the birth of the new China, accounting scholars instigated a nation-wide debate about the national characteristics and the scientific virtues of bookkeeping methods (Chen, 2006). The Ministry of Finance was established within the Central Government in 1949 as the department in charge of accounting affairs, and commenced to unify the variety of accounting systems inherited from the old society.

New accounting system considered the characteristics of State-operated economy and the demands of State's finance and financial management. It was a mixture of scientific methods which were taken from Western accounting theory and Soviet-type accounting

The private sector had disappeared in the 1950s, and the Chinese national economy Relied mainly on state-owned companies (SOE). The CPA system also came to be canceled. Accounting issues were the responsibility of the Accounting Rule Division created in late 1949 at the Finance Ministry, which gradually introduced the unified accounting system devised by the Soviet Union. This accounting system relied on physical quantities and had the following objectives:

· determining production quotas,

· controlling limited resources,

· allocating scarce resources between production activities, and

· reporting on production results and State funds.

¶ Starting in 1966, debit-credit bookkeeping was abolished and replaced by the newly minted increase-decrease method in the merchandising sector. Shortly after the birth of the increase-decrease method, the Cultural Revolution quickly swept the country. The increase-decrease bookkeeping uses the words "increase" and "decrease" as bookkeeping labels, and records increase in any account on the left side and decreases on the right side in order to maintain a balance between fund applications and sources. With accounts classified according to the accounting equation and opposite recording rules for asset accounts and liability/equity accounts, debit-credit bookkeeping is able to maintain a balance between debits and credits in a single transaction, in all transactions together, and in account balances (Chen).

Mao Zhedong initiated the Cultural Revolution in 1966, following five years of natural disasters during which the Chinese economy suffered enormous losses and agriculture and manufacturing almost totally collapsed. The stated purpose of the Cultural Revolution was to eliminate all traditional Chinese culture; the real purpose, however, was to cleanse the Communist Party of all of Chairman Mao's political opponents. This Revolution completely destroyed the weak Chinese economy. Production of goods and services, government affairs, and education all came to a halt. Development of the accounting system was suspended.

O ~~An~~other significant moment s in the Chinese Accounting Standards occurred in 2000, 2006 and 2014. — was released as One ¶

In 2000, The Old PRC GAAP. It The Accounting Standards for Business Enterprises ~~was~~ included ~~released with~~ 16 accompanying specific standards and relevant supplementary rules.

In 2006, The New PRC GAAP was released. The Ministry of Finance issued a new set of Accounting Standards for Business Enterprises (ASBEs), which are substantially converged with the IFRS. This was composed of a Basic Standard, 38 specific standards and application guidance.

In 2014, the Revision of The New PRC GAAP was released. The basic standard and five specific accounting standards were amended, and three new standards were released. One ¶ w/ 2 cites

III. Current Accounting Standards

Instead of being phased in gradually over time as was the case with many other countries' adoptions of standardized procedures, China is choosing to adopt the main standards essentially in one go. Quite how this will pan out is difficult to tell and may be a question which only time has the answer to. However, this initial shift in standards is unlikely to be the end of the Chinese accounting reforms and so changes are expected to be ongoing. That convergence is a process and that the goal of fully uniform accounting standards between Chinese firms and those applying IFRS is attainable in light of the progress that has been made, though no mention is made of any additional convergence procedures. (Citation)

Taken as a whole the majority of the changes are in line with IFRS but the differences that do exist represent China's unique position in the global economy. This includes a prohibition of reversing an asset impairment decision; financial statements incorporating certain government grants; and related party disclosures between certain state-owned enterprises. Prior to the reforms Chinese Accounting Procedures had one basic standard and sixteen specific standards, most of which were implemented fairly recently, between 1996 and 2001. This will have to be increased considerably to conform to IFRS standards. Indeed, 22 additional specific standards have been added to CAS, more than double the original number, with the initial sixteen also experiencing some modifications. (Citation)

IV. Scope of Chinese Accounting Standards

The term China generally accepted accounting principles (GAAP) refers to Chinese Accounting Standards (CASs) issued by the Accounting Regulatory Department of the Chinese Ministry of Finance (MoF), which is the sole authority that sets accounting standards in China. The CASs for enterprises mainly consist of two sets of accounting standards: the Accounting Standards for Business Enterprises (ASBEs) and the Accounting Standards for Small-Sized Business Enterprises (ASSBEs). (Citation)

The ASBEs are the Chinese counterpart of International Financial Reporting Standards (IFRS); the ASSBEs are the counterpart of IFRS for SMEs. The ASBEs enjoy an increasingly wide application since their issuance in 2006. Currently, the ASBEs are compulsorily applied by all companies listed in mainland China, all Chinese financial institutions, and all large-size state-owned enterprises. More and more, other enterprises are adopting the ASBEs on a compulsory or voluntary basis. Due to the wide application of the ASBEs, the acronym of CASs is officially used to refer to the ASBEs. (Citation)

The ASSBEs are the counterpart of IFRS for SMEs, providing unified standards for small-size enterprises. The ASSBEs use the ASBEs as a reference but are more similar to tax laws in terms of their tax calculation methods, which simplify the process of making adjustments between accounting standards and tax rules. Small-scale enterprises can choose to adopt either the ASBEs or ASSBEs. (Citation)

V. Comparison of Chinese GAAP, IFRS and U.S. GAAP

Although the new PRC GAAP converged with IFRS, it cannot be assumed that the policies adopted by the latter will comply with the new PRC GAAP in all cases. The financial information disclosed according to the new PRC GAAP does not match always the IFRS ones, particularly in the case of consolidated financial statements. The following situations may occur:

US GAAP & PRC GAAP have each been converged with IFRS.

One ¶

- Some options that are allowed according to IFRS, are not in the new PRC GAAP. New PRC GAAP contain specific obligations for some of the problems commonly found in China, where IFRS do not have regulations. Some specific needs contained in IFRS, about issues not commonly found in China, are covered by general principles in new PRC GAAP, rather than being included in specific standards. (Citation)

	Chinese Accounting Standard (CAS / PRC GAAP)	International Financial Reporting Standards (IFRS)	US Generally Accepted Accounting Standards (US GAAP)
Introduction	CAS is a set of accounting rules and standards for financial reporting in China	IFRS is a set of accounting rules and standards for financial reporting used in over 110 countries and many other countries are converging to IFRS (including China)	US GAAP is a set of accounting rules and standards for financial reporting used in the United States of America
Performance Elements	Revenue or Expenses Assets or Liabilities, Gains or Losses, Comprehensive Income	Revenue or Expenses Assets or Liabilities	Revenue or Expenses Assets or Liabilities Gains or Losses Comprehensive Income
Impairment of Assets	One-Step Test of Impairment: Once impairment has been recognized it cannot be restored	Two-Step Test of Impairment	One-Step Test of Impairment: once impairment has been recognized it cannot be restored
Estimation of Inventory Cost	Last In, First Out ("LIFO") First In, First Out ("FIFO") Weighted-Average Cost	Last In, First Out ("LIFO") Weighted-Average Cost	Last In, First Out ("LIFO") First In, First Out ("FIFO") Weighted-Average Cost
Inventory Reversal	Prohibited	Can be made over certain conditions	Prohibited
Capitalization of Development Cost	Can be capitalized under certain conditions	Can be capitalized under certain conditions	Prohibited
Depreciation Methods and Expenses	Straight-Line Method Accelerated Methods (for some industries not all)	Straight-Line Method Accelerated Methods Unit of Production Method	Straight-Line Method Accelerated Methods Unit of Production Method
Interest & Dividends Expense	Classified as a Financing Cash Outflow	Classified as an Operating Cash Outflow <u>OR</u> Financing Cash Outflow	Classified as an Operating Cash Outflow
Asset Valuation	Historical Cost	Historical Cost or Fair value for Valuing Assets	Historical Cost Re-evaluation of Assets (under certain conditions)

Source: ? Citation?

2 sentences per ¶

Impairment of Assets: CAS & US GAAP states that once impairment has been recognized it cannot be restored, while IFRS uses a Two-Step test of impairment. (Citation)

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Estimation of Inventory Cost: Under CAS, IFRS & US GAAP, there are three key methods to report inventories: FIFO, Weighted Average Cost and LIFO (which is not permitted under IFRS). All methods are permitted under CAS, but they all have a different impact on a balance sheet and ratios.

In respect to

- Depreciation Method and Expenses, there are three....
- Straight-Line Method; This method is permitted under CAS, IFRS & U.S. GAAP. This Straight-Line Method is probably the most common approach for many enterprises. It consists of subtracting the expected residual value of expenses divided by its useful life. This method allocates the expense proportionally over the expected lifetime of the assets.
- Accelerated Method; This method is fully permitted under IFRS & U.S. GAAP. However, under CAS, this method is permitted only if a business is in one of the following industries;

  1. Biopharmaceutical Manufacturing
  2. Manufacturing of Special Machinery or Transportation Equipment
  3. Manufacturing of Electronic Devices
  4. Manufacturing of Instruments & Meters, Software Production and Information Technology.

  This method is similar to the Straight-Line Method, but it allows for allocating greater expenses earlier in the year, which will have a greater impact on financial statements and a company's tax filing.
- Unit of Production Method; This method is only permitted under IFRS and U.S. GAAP.

Use narrative style, that is ¶s

VI. Expectation of Adoption of IFRS in China

There were further developments after the mandatory adoption of New PRC GAAP, on 1st January 2007, to improve the convergence with IFRS. ~~After~~ Since 2007, there have been a series of documents, in order to assess the status of convergence of Chinese Accounting standard.

(Citation)

The "Roadmap for Continuing and Full Convergence of the Chinese Accounting Standards for Business Enterprises with the International Financial Reporting Standards", published by Chinese MOF, on September 2, 2009 documented that China would have tried its best to continue the convergence process. The final goal was to reach a full convergence of Chinese New PRC GAAP with IFRS in a short period of time. (Citation)

In 2012, Chinese MOF also founded the Asian-Oceanian Standard Setters Group (AOSSG), an association of Asian-Oceanian Accounting standard setters. This Roadmap is crucial to have a better understanding of the steps that came after the first convergence process' step. (Citation)

In 2014, the Chinese MOF issued three new ASBEs (CAS 39 Fair Value Measurement, CAS 40 Joint Arrangements, CAS 41 Disclosure of Interests in Other Entities) and revised five of them47(KPMG, 2014). Moreover, several Exposure Drafts in 2015 and 2016 were issued, which are in continuing convergence with IFRS. The most recent development occurred on November 2016, when the MOF and the IFRS Foundation signed a joint statement in Beijing, on the Trustee's final meeting. (Citation)

VII. Summary & Conclusions

The adoption of the New PRC GAAP has become compulsory for all listed companies, for non-listed and for public financial companies, marking a period of fundamental transition in the Chinese race towards an ever-greater internationalization and a global development. From the date of the introduction of these new principles to the present, China has been shown to be seriously committed to extending its adoption to small companies as well, showing in line with the prospect of international economies. In fact, this reform has had an innovative and consistent value.

Since New PRC GAAP was adopted, its application coverage has been gradually expanding. Up to 2014, A-share listed companies, banks, insurance enterprises, securities enterprises and central state- owned enterprises have already adopted New PRC GAAP. Some medium and large-sized enterprises in certain provinces or cities have also been required to adopt New PRC GAAP. However, there are still a number of enterprises that are currently implementing Accounting Regulations for Business Enterprises and related accounting standards (commonly referred to as Old PRC GAAP), including many foreign invested enterprises (FIEs) and private enterprises. These enterprises will face the challenge of GAAP conversion. Gaining an understanding of New PRC GAAP, and the extent to which it differs from Old PRC GAAP, will be an important part of a successful conversion.

VIII. References/Bibliography.

Separate page

Chen cited but on list below,

- Mao's Cultural Revolution in 1967: The Struggle to Seize Power
- Chinese Accounting Standards
- Accounting Standards for Business Enterprises (ASBEs); and
- Accounting Standards for Small Business Enterprises (ASSBEs).

Incomplete citations

More citations needed