CONSIDERATIONS ON CHINA’S ACCOUNTING SYSTEM – A RISING COUNTRY TRYING TO BECOME AN EXAMPLE OF SUSTAINABLE DEVELOPMENT

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Abstract

China, a country with an economy and population whose values exceeded all expectations over the last century, still makes considerable efforts to answer several calls from policy makers to develop responsibly in terms of industrialization, used resources and their reuse, economic restructuring, environmental protection and health etc. The major goal of China, the fact that its economy could become leader until 2030, its direct involvement in The Global Markets Project, and other items, make the study of national particularities of the accounting system of this country to be a topic of great interest.

The fact that China has become a key pawn in the economy and world politics, reflected it in the accounts also. Development of cross-border transactions, capital markets, tax, multiple ownership of economic entities, all of these and not only, lead to the need for convergence with international accounting standards.

Therefore, we try by means of this paper, to approach a series of issues related to past, present and likely future of the Chinese accounting system, how the system will influence and will be influenced by the social, economic and political environment.

Key-words: Chinese accounting system, normalization, convergence, CAS, IFRS.

Clasificare JEL : M41, M48, N10.

1. Introduction

China is the subject of an extensive process of internationalization of accounting that heads extremely fast toward completion. As with many other national accounting systems, the Chinese accounting system is the result of forces (social, political, economic, educational) that acts internally and externally.

Of these, if we refer to the economic vector, we can say that today is marked by The Global Markets Project, a project which is a conglomerate of the International Institute for Sustainable Development and the Chinese Ministry of Commerce and targeting changes in next period in the economic, political, social, and global changes that are intended to influence China’s decisions regarding production, consumption, trade and infrastructure, so that the problems facing sustainable development to be removed in the following years [1].

In this context, the present paper proposes a dynamic analysis, but also a content one, and will highlight a number of significant aspects of past, present and future of Chinese accounting.

2. The evolution of Chinese accounting system

The table below shows the steps considered by specific literature to be the most significant reference in the preliminary development of Chinese accounting system focused on the evidence in simple entrance:

<table>
<thead>
<tr>
<th>Nr. crt.</th>
<th>Time period</th>
<th>Phase name</th>
<th>Characteristics</th>
<th>Objectives</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>2000 B.C. – 1500 B.C.</td>
<td>Kuji phase (preliminary/primary accountant)</td>
<td>- recording of transactions in the records / registers;</td>
<td>- quantify the achievements of princes and dukes;</td>
</tr>
<tr>
<td>2.</td>
<td>1500 B.C. – 1000 B.C.</td>
<td>Divination Phase</td>
<td>- increases the level of complexity of accounting;</td>
<td>- register rewards received by officials, or offerings dedicated to the gods or</td>
</tr>
</tbody>
</table>
Double entry accounting, DEB myth is so deeply rooted in ancient literature that is quite difficult to clarify whether this occurred:
- **in response** to needs for processing and obtaining information for decision-making and the check in a new economic and social order;
- **as instrument** necessary and sufficient to be presented both features in a single system.
The idea could be debated again in the context contradictions and similarities between successful development of his late Imperial China and emerging evidence of the duality limits stated in the accounts registers and Chinese accounting [2].

Therefore, we try by means of the following table to expose a summary of the evolution of Chinese accounting double entry focused on periods that followed those previously presented.

**Table no. 2. Aspects concerning the evolution of the Chinese accounting system from the 10th century to the beginning of the 21st century**

<table>
<thead>
<tr>
<th>Nr. crt.</th>
<th>Time period</th>
<th>Phase name</th>
<th>Characteristics</th>
</tr>
</thead>
</table>
| 1.       | 960 – 1179    | Song Dynasty Phase | • the data combined prepared procedures of official bookkeeping reports were explicit in financial and treasury document grains, and were brought into the official document system, thus stepping further toward standardization;  
• use balance accounting method in four columns, Sizhu, whose specific equation was: $J (beginning balance) + X (newly received) − K (disbursement) = S (ending balance)$ [3]; |
| 2.       | 1368 – 1644   | Ming Dynasty Phase | • method of record „three-feet” (15th century), method that used:  
  ○ a double entry for recording receivables and transfers and  
  ○ a simple entry for cash transactions; |
| 3.       | 1644 – 1911   | Qing Dynasty Phase | • method of record „three-feet”, the first method that used double entry accounting principles, assuming double entry recording of all transactions:  
  ○ operations both cash and non-cash ones, were registered in correspondent accounts in both the journal and the ledger;  
  ○ final products consist of two accounting reports: report *caixiang report* (profit and loss statement) respective *cungui report* (balance) [4];  
• method of record „three-feet” was followed by method „four-feet” (18th century);  
• stage ended with unprecedented fiscal and administrative reforms;  
• from the 19th century are widely used methods of double entry |
<table>
<thead>
<tr>
<th>Year Range</th>
<th>Phase</th>
<th>Events</th>
</tr>
</thead>
</table>
| 1911 – 1949 | Nanjing Provisional Government Phase | • Accounting services are summarized as follows:  
  o General accounting services (which later became public accounting services);  
  o Special accounting services (accounting services referred to later in the sphere of state-owned enterprises and other public institutions) [2];  
  o A number of laws are developed and issued, such as:  
    o Accounting Law - 1914, republished in 1935;  
    o Accounting Law Firms - 1948;  
    o Accountants Law - 1945;  
• Regulatory central accounting body is established, namely Ministry of Finance; |
| 1949 – 1979 | Mao Phase | • The establishment of Public Republic of China;  
• Accounting Systems Division is created within the Ministry of Finance;  
• Development of uniform accounting systems for each branch of the economy in which the state owned capital;  
• Accounting is strongly influenced by ideological principles focused on class struggle, central planning and public power, applicable accounting principles in West being prohibited [5];  
• In the period 1950 - early 1990, it adopted the Soviet model of planned economy and the Russian accounting system, which assumed control of the use of state funds entrusted to businesses, combining financial accounting management accounting [6]; |
| 1979 – 2000 | Deng Phase | • The concept of socialist market economy is born;  
• Accounting becomes a technical and neutral science without national boundaries, a set of principles in the West being adopted [5];  
• Accounting Standards Division is reorganized and renamed Department of Business Management Accounting;  
• The Accounting Law of Public Republic of China is issued in 1985, developed to meet the new economic realities;  
• The emergence of two stock exchanges will require a proper accounting system with a few generally accepted systems - Accounting Standards for Business Enterprises (ASBE), 1993;  
• Therefore, the accounting reform is initiated, aiming that the Chinese Accounting Standards would be nearer to International Accounting Standards by assimilation equation (\( A = D + CPR \)) the content of financial statements, accounting integration methods such as double-entry method of flow and credit, methods of calculating production costs, depreciation methods of property etc.;  
• After the foundations of building a financial integrated reporting system are set; |
| 2000 – 2007 | Convergence Phase | • Development of standards to follow international accounting trends becomes the main objective;  
• 2006 - a new set of Accounting Standards for Business Enterprises (ASBE), requiring all listed companies their implementation from the 1 January 2007; |

3. About the accounting profession

Although China has to his credit over 5000 years of history, the accounting profession has emerged after the bourgeois-democratic revolution of 1911, which overthrew the Qing Dynasty, the main purpose being to serve the development of the national economy.

With the founding of the Popular Republic of China in 1949, the economy has become one of the planned type. During this period, accounting bodies and all staff have been in close contact with central and local authorities, with no independent accountants or independent institutions of accounting. Since the services provided by professional accountants were not widely used, there has been a stagnation of the development of the accounting profession [7].

Since 1980, in the context of outward opening political reforms, interest in building a national accounting profession has become increasingly pronounced.
Thus, in 1993 it issued Chartered Accountants Act. In addition, the roles of professional accountants were stipulated and recognized throughout the legal system of China, namely thought rules such as: Commercial Entities Law, Securities Law, Insolvency Law, the Law on State Enterprises and the Law on Commercial Banks.

The body representing the accountant profession in China was established in 1988, namely the Chinese Institute of Certified Accountants Public (ICAP) self-disciplinary organization whose tasks are: review and authorization of accountants, providing services to its members, monitoring of professional ethics and quality of services provided by members (professional accountants) [8].

As with many other national accounting systems, one of the disadvantages of the Chinese accounting system is that the body representing the accounting profession has no active role in the development and establishment of accounting standards, this power is solely the responsibility of the Ministry of Finance.

By year 1995, the audit profession was represented by an independent organization, independent from the body of the accounting profession, known as the China Association of Certified Public Auditors (CACPA). While the Institute of Certified Public Accountants, under the jurisdiction of the Ministry of Finance has responsibility for monitoring audit activities in the field of private companies, CACPA, under the authority of the State Auditing Administration, have responsibilities in the state enterprises audit. In 1995 the two organizations merged, retaining the name of CICPA.

At present, the audit profession in China is represented by the Auditing Standards Board (CASB) established in CICPA structure, with role in the development of auditing standards, which are intended to be comparable to standards issued by the International Federation of Accountants (IFAC).

4. Accounting normalization in China

In China, responsible for the formulation, promulgation and administration of accounting regulation is the Ministry of Finance (MOF). To ensure an effective platform for developing and implementing accounting standards, the Ministry of Finance created in 1998, in its structure, an Accounting Standards Board composed of representatives of major Chinese investors. The purpose of this committee is to provide advice on overall planning, structure and development of accounting standards, the choice of policies and implementation of accounting standards [9].

Therefore, unlike Western practices, in China practice for setting mandatory accounting rules is not the responsibility of Accounting Society of China (ASC), or the Chinese Institute of Certified Public Accountants (ICAR).

However, both Accounting Society of China (ASC) and the Chinese Institute of Certified Public Accountants (ICAR) are responsible for the management, governance, supervision, reform and development of the accounting profession in China. Chinese Institute of Certified Public Accountants (ICAR) also assumes a certain administrative authority delegated by the Ministry of Finance (MOF) to serve as a bridge between government and accounting professionals.

The main government institutions with responsibilities in the sphere of accounting, taxation and audit and main functions are presented in the table below:

<table>
<thead>
<tr>
<th>Nr. cert.</th>
<th>Official body</th>
<th>Functions/Responsibilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Ministry of Finance (MOF)</td>
<td>• formulation, promulgation and administration of accounting regulations; • does not act directly in firms;</td>
</tr>
<tr>
<td>2.</td>
<td>State Administration for Taxation (SAT)</td>
<td>• levying taxes, issuing the special forms (invoices) fiscal control;</td>
</tr>
<tr>
<td>3.</td>
<td>State Administration of Industry and Commerce (SAIC)</td>
<td>• licensing activity and the annual review of business activity. (Income statement and balance sheet);</td>
</tr>
<tr>
<td>4.</td>
<td>External Audit Company (CPA)</td>
<td>• the annual external audit obligatory;</td>
</tr>
<tr>
<td>5.</td>
<td>Ministry of Commerce (MOC)</td>
<td>• approving the distribution of dividends.</td>
</tr>
</tbody>
</table>
With the implementation of economic reform, China’s Ministry of Finance has been devoted to the development of accounting standards that would improve financial reporting quality in relation to Chinese firms. To achieve this goal, MF initiated a project, with deadline the year 2005, for achieving convergence of Chinese Accounting Standards (CAS), with accounting standards internationally recognized (IFRS).

Between 1992 and 2006, the MF has prescribed a series of four accounting regulations applicable to companies whose A type shares were listed. Thus, the development of accounting standards in achieving convergence can be divided into four major steps, briefly described in the table below [11]:

**Table no. 4. The main stages in development of ASBE Synthesis**

<table>
<thead>
<tr>
<th>Stage</th>
<th>Period</th>
<th>Characteristics</th>
<th>Issued regulations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stage I</td>
<td>1993-1997</td>
<td>• China’s revolutionary changes in accounting because introduces a market-oriented accounting pattern;</td>
<td>• experimental system of accounting for joint stock companies and limited liability companies;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• accounting standard for business enterprises (with role of conceptual framework and guide for developing new accounting standards);</td>
<td>• 13 branch accounting systems, for unlisted companies and the 2 systems based on the property;</td>
</tr>
<tr>
<td>Stage II</td>
<td>1998-2000</td>
<td>• replacement of the accounting system in 1992;</td>
<td>• accounting system for joint stock companies and limited liability companies;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• 10 specific accounting standards;</td>
</tr>
<tr>
<td>Stage III</td>
<td>2001-2006</td>
<td>• replacement of the accounting system in 1998;</td>
<td>• the accounting system for business enterprises</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• 16 specific standards;</td>
</tr>
<tr>
<td>Stage IV</td>
<td>2006 - present</td>
<td>• crowns the efforts of the Chinese authorities in China accounting convergence with international accounting practices.</td>
<td>• Accounting Standards for Business Enterprises (ASBE).</td>
</tr>
</tbody>
</table>

Thus, in February 2006 the **Accounting Standards for Business Enterprises (ASBE)** are issued, in force since 1 January 2007. At that time, ASBE included: a baseline (the revised one issued in 1992), and 38 specific standards (CAS), which replaced the accounting system in 2001 and the 16 standards previously issued.

Even if the ASBE application was initially requested to listed companies, other entities were encouraged to apply it also. The actual data of adopting ASBE by various companies are listed below [12]:

**Table no. 5. Calendar of adopting ASBE by different types of entities**

<table>
<thead>
<tr>
<th>Type of business</th>
<th>With effect from 1 January</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2007</td>
</tr>
<tr>
<td>Listed companies</td>
<td>✓</td>
</tr>
<tr>
<td>Insurance societies</td>
<td>✓</td>
</tr>
<tr>
<td>Investment companies and Investment funds</td>
<td>✓</td>
</tr>
<tr>
<td>Banks (other than banks operating in regional development field)</td>
<td>✓</td>
</tr>
<tr>
<td>Banks operating in regional development field</td>
<td>✓</td>
</tr>
<tr>
<td>Large and medium enterprises (other than state-owned enterprises), which are recorded:</td>
<td></td>
</tr>
<tr>
<td>- Shenzhen Stock Exchange</td>
<td>✓</td>
</tr>
<tr>
<td>- In provinces Shanxi and Yunnan</td>
<td></td>
</tr>
</tbody>
</table>
In the near future, it is expected that all large and medium enterprises to adopt the ASBE. Once this target is reached, the Ministry of Finance will repeal all accounting branch systems (issued in 1992), the 16 accounting standards issued in 2001 and other related rules. This process will be completed by issuing a single set of accounting standards aimed at promoting sustainable development of enterprises, and improving capital markets.

Characteristics of Accounting Standards for Business Enterprises consist mainly of:

- ASBE was designed as a uniform accounting system aligned with international standards, designed to meet the requirements of China’s socialist market economy;
- these standards are incorporated in the legal system;
- applying the accruals convention and compliance with principles such as: the permanence of methods, the linking of expenditure to income and objectivity quality are required;
- in terms of assets, in their evaluation historical costs are used, with the mention that there should be distinguished between revenue expenditure and capital expenditure; are classified in current and non-current;
- stocks can be measured by conventional methods, including LIFO;
- fixed assets can be amortized by using the straight-line method or methods based on activity; in certain situations, accelerated amortization method is accepted;
- intangible assets, including goodwill, are recognized and amortized during the periods when the obtaining of economic benefits is estimated;
- capital consists of invested capital, capital reserves, reserves and surpluses retained earnings; invested capital is the actual value of the issued shares and government investment;
- capital reserves include the share premium, increases resulting from the revaluation of assets, capital donations; surpluses resulting from reserves refers to undistributed earnings affected to a purpose; retained earnings refers to undistributed earnings, notwithstanding any purpose;
- revenues are determined on an accrual basis, in respect of projects/long-term contracts, revenues can be recorded either by the completion of the works, or are based on the percentage method of compliance;
- expenses are recorded on an accrual basis on account of actual costs; companies using standards based on cost estimations must register deviations from the actual costs at the end of current month;
- The set of financial statements comprise: the balance sheet, income statement, statement of changes in financial position (or cash flow), any detailed statements of items, and notes.

Branch accounting systems are represented by the following structures:

- accounting system for industrial enterprises;
- accounting system for commercial enterprises;
- accounting system for transport companies;
- accounting system for railway undertakings;
- accounting for the airlines undertakings;
- accounting system for transport undertakings (Post and Telecommunications);
- accounting system for hospital enterprises;
- accounting system for construction enterprises;
- accounting system for real estate enterprises;
- accounting system for agricultural enterprises;
- accounting system of financial institutions;
- accounting system for insurance companies;
- accounting system of foreign economic cooperative societies;

Systems based on the property are the following two:

- accounting system for foreign investment enterprises;
- accounting system of limited liability companies.

5. CAS –IFRS Convergence

During the process of developing new Chinese Accounting Standards (CAS), the Chinese Accounting Standards Committee (CASC) involved the International Accounting Standards Board (IASB) to confirm the extent to which the new CAS are convergent with IFRS. This process culminated in 2005 with the signing of the CASC and IASB of a joint statement which said that the new CAS reached convergence with IFRS.
Convergence is a dynamic process of achieving substance coherence between national accounting standards and IFRS. Convergence, however, does not mean adopting IFRS directly, nor their actual translation. For example, in the new CAS convergence to IFRS, a limited number of specific differences have been noted and highlighted in the Statement of Convergence from 2005, such as those relating to disclosure on related party relationships and transactions and canceling losses impairment. For these situations, CASC considered IFRS approach as inadequate to economic realities of the PRC.

Given that the new CAS are converged with IFRS, a direct or approximate correlation may already be established between individual Chinese and IFRS standards, only a few examples of such correspondences are the following [13]:

- IFRS 1 First-time Adoption of International Financial Reporting Standards / CAS 38 First-time Adoption of Accounting Standards for Business Enterprises;
- IFRS 2 Share-based Payment / CAS 11 Share-based Payment;
- IFRS 3 Business Combinations / CAS 20 Business Combinations;

Also, there are situations in which such matching may not be established. For example, the international standardization system acts IFRS 5 Non-current Assets Held for Sale and Discontinued Operations, but in China’s accounting system, there is no specific standard - current assets held for sale. However, these requirements can be found in the provisions of CAS 4 Tangible fixed assets, which require that the carrying amount of a fixed asset to be adjusted if the asset is held for sale.

6. Conclusions

In order to understand the current state of the Chinese accounting system, there must be studied in detail its evolution, from its first organizational forms from antiquity to the present status, the one of convergence, where Chinese accounts can be set in. Thus, it appears that the country’s political and economic evolution and its impact on accounting practices resulted in the final accounting transformation into an instrument of the Cultural Revolution and China’s opening to the outside.

The fact that China’s share in the economy and related global policy grows exponentially every day, developments in financial markets and beyond, require that this phenomenon of internationalization, to reflect on the accounting system also. An example of this is the fact that the Chinese authorities have imposed on companies listed on stock exchanges in Shenzhen and Shanghai to apply IFRS.

However, even if China has proposed to implement IFRS, there will be a while until information could be comparable to those in Western countries, as mere compliance with rules is not enough if they are not fully accepted and recognized socially, politically and culturally.

Thus, scientists have identified that a major problem is the lack of consistent interpretation of the requirements of the standards. Given the fact that China is a transition economy, the infrastructure necessary to sustain a credible financial reporting is just emerging and, therefore, the formal convergence of accounting standards and audit took place in China has led the convergence integrated accounting practices.

ASBE, as they were issued in 2006, aimed, inter alia, to improve the comparability of financial information, the separation of accounting treatment from the fiscal ones and assurance of convergence with internationally accepted accounting practices.

It is important to note that with economic reforms, a new audit system has appeared, the purpose of audits is no longer represented by verifying compliance with tax obligations of a company, but finding the truth and fairness of financial statements of a company. Currently, most companies in China are subject to annual audit conducted by the accounting firm authorized, registered in China.

Regarding the report accounting/taxation, although the market economy is under construction and companies gradually gain autonomy, inherent in the old accounting system is experiencing due to the importance that is given to taxation. Between accounting and taxation is determined as a ratio of quasi dependence [14], since taxable income is determined mostly on the basis of accounting with a number of adjustments provided for tax regulations in force.

Tax regulations tend to affect the financial statements, and this often prevents fair presentation of financial information. To meet the tax authorities regarding the recognition of taxable income and deductible expenses, specialists, preparing financial statements, often tend to deviate from the applicable financial reporting standards, preferring to meet tax regulations. As a result, the treatment of certain items in the financial statements may differ from the prescribed accounting standards of Chinese, the reason of these discrepancies are represented by accounting attempts to reduce tax liabilities.
Therefore, on long term, the adjustment of discrepancies between accounting and tax mechanisms, as well as CAS - IFRS convergence will be likely elements that will form the basis for building an effective Chinese accounting system and fully consistent with the level of development of the national economy.

7. References and bibliography