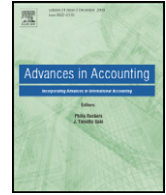




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The impact of the new Accounting Standards for Business Enterprises (ASBE) on financial results of mainland Chinese listed companies

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ABSTRACT

Effective 1st January 2007, 38 new Accounting Standards for Business Enterprises (ASBE) had become applicable to listed companies in mainland China. Research based on these latest standards will help us understand the current accounting harmonisation process in China. Previous studies, though rather scarce, had compared financial statements of companies simultaneously being listed on the mainland and Hong Kong. However, the very recent impact of the new ASBE has not been taken into account. Therefore, the present study focuses on domestic Chinese companies after implementation of the new ASBE. The financial figures of each item reported under the old Chinese Accounting Rules and Regulations and the new ASBE were collected in pairs and were analysed. Except for the test results on total assets and shareholders' equity, the other results revealed no significant differences between the paired figures of net assets per share, operating revenue, profit before tax, net profit, net profit after extraordinary gains and losses, basic earnings per share, net cash flow from operating activities and the per share value.

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1. Introduction

Consistent with the trend of international capital markets, there is growing demand from accounting users for financial information which demonstrates a high level of objectivity, accuracy, comparability and transparency in mainland China. Refinement of the accounting standards is necessary in order to meet increasingly demanding global requirements. Harmonisation of reporting standards does not only bring transparency and instils confidence among foreign investors; it also reduces the costs of raising capital by enterprises and alleviates the risks of financial crises (Deloitte Touche Tohmatsu, 2007).

In the past, many attempts of accounting reform have been undertaken in China to keep up with economic development. On 15th February 2006, the Ministry of Finance of China had issued a series of new and revised Accounting Standards for Business Enterprises (ASBE) comprising a basic standard and 38 specific accounting standards of which 22 were newly promulgated. These standards had become effective starting 1st January 2007 for listed companies on the mainland. The implementation of this new system represents substantial convergence of the ASBE with the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS), with due consideration being given to the unique situation in China. The new ASBE not only cover the recognition,

measurement, presentation and disclosure of most general transactions and events, but also provide guidance for certain specific transactions and industries. The new standards have also brought in some new accounting principles and measurement requirements.

As can be seen from above, the harmonisation process in China has been progressing rather feverishly in the recent years. However, in the academic arena of the Western world at least, up-to-date research which focuses on this area remained rather scarce. Most of the available studies, analyses and commentaries were published during the 1990s and early 2000s (e.g. Chen, Gul, & Su, 1999; Chen, Sun, & Wang, 2002; Chow, Chau, & Gray, 1995; Ding, 2000; Ji, 2001; Lin, 1998; Lin & Chen, 2000; Lin & Wang, 2001; Tang, 2000; Winkle, Fenwick Huss, & Chen, 1994; Xiang, 1998). There have only been a few studies on changing accounting standards on the mainland during the past three years or so. Haverly (2007) published a case concerning China Eastern Airlines which is simultaneously listed in mainland China, Hong Kong and the US and therefore prepares three sets of financial statements using Chinese accounting standards, IFRS and US GAAP. Nevertheless, the paper is actually a case for students and does not provide much analytical insights into accounting standard changes.

Biondi and Zhang (2007) made a comparative study on the IFRS and the Chinese ASBE promulgated in 2006. They analysed the two systems based on the dualistic characteristics of two accounting systems namely static (fair value) and dynamic (matching based). Their excellent analysis included detailed studies of the individual accounting standards of both systems from historical, economic and political economy perspectives. Unfortunately, they did not employ empirical quantitative data and therefore we are unable to verify their

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propositions. Also, their focus is only on accounting for business combinations so that we are unable to speculate the situation of convergence of the other standards.

A recent publication which had actually addressed the issue of harmonisation in China is the study conducted by Ip and Noronha (2007). They performed a quantitative analysis to compare the financial reports of 30 Chinese companies simultaneously issuing H-shares in Hong Kong and A-shares in China. However, their research was conducted prior to the implementation of the new ASBE and therefore the impact of the new standards was not captured. They called for further studies so as to assess the real effectiveness of the new standards. Therefore, the present study aims to fill up the lacuna by analysing the impact of the new ASBE on selected financial statement items under Chinese domestic A-share reports, with a hope to shed some light on the most current harmonisation trend on the mainland.

2. The evolution of accounting standards in china

Since the founding of the People's Republic of China in 1949, the Uniform Accounting System, based principally on the Soviet Union's system of accounting, was developed to facilitate central control and the implementation of economic policy for a socialist economy (Blake, Gao, & Wraith, 2000). Following the economic reform in 1978 and to match up with the policy of encouraging foreign investments in China, the country realised that the accounting system had to change its orientation from providing information for state planning and control to providing information useful for managerial decision-making (Winkle et al., 1994). The rigid Soviet-inspired system had become obsolete with the implementation of Deng's 'Open-Door' policy.

Between now and then, the accounting system in China had experienced numerous revisions and reforms. In response to increasing foreign investments in China, the Ministry of Finance issued the Regulations on Accounting System for Sino-Foreign Joint Ventures in 1985. These regulations had introduced Western accounting practises to firms operating in China for the first time. Differing significantly from the accounting standards under the centrally-planned system, the 1985 regulations had adopted internationally accepted accounting principles to the maximum extent possible under China's socialist economy (Blake et al., 2000). Also in 1985, the National People's Congress enacted the Accounting Law which defined the functions of accounting, the organisation of accounting work, the powers, duties and legal responsibilities of accounting personnel. Accounting systems were launched to provide operational methods, procedures and financial reporting requirements for different enterprises. The two-tiered accounting systems, one for foreign joint ventures and the other for national enterprise units, continued to operate (Chen et al., 1997; Blake et al., 2000).

The accounting system in China had undergone another fundamental change after the establishment of the Shanghai and Shenzhen Stock Exchanges in the early 1990s. In 1992, listed companies which were previously authorised to issue A-shares only to domestic investors were allowed to issue B-shares to overseas investors. State-owned enterprises were also transformed into shareholding entities with limited liabilities through corporatisation and could

issue listed shares to the public (Xiang, 1998). The entire landscape of China's market system had changed drastically and new accounting standards became urgently necessary.

Consequently, in 1992, the Ministry of Finance promulgated new accounting standards to replace the Soviet accounting model in its entirety and to merge the dual accounting systems into one common system. The Accounting Standards for Business Enterprises (ASBE), being the fundamental standards, were issued in the same year and came into effect on 1 July 1993. The standards superseded all accounting regulations issued formerly and were applicable to all Chinese enterprises regardless of ownership structure (Chen et al., 1997; Xiang, 1998). Although the Chinese government had been paying substantial effort in harmonising the Chinese accounting standards with their international counterparts, significant differences between the two standards still existed. This had been reported in the study of Chen et al. (1999). In view of the incongruity, from 1999 onwards, numerous changes, cancellations and additions to the existing accounting system took place, including amendments to the Accounting Law, issuance of new regulations for financial reporting and the making of new standards.

The situation began to stabilise in 2006 when the Ministry of Finance issued a series of new and revised Accounting Standards for Business Enterprises (the 'new ASBE'). The new ASBE include the revised Accounting Standard for Business Enterprises—Basic Standard (the 'basic standard'), 22 newly promulgated standards and 16 revised standards. The new system became effective starting 1 January 2007.

3. Overview of the new ASBE

The new ASBE represent convergence with IFRS to a large extent. Most of the newly issued and revised standards make references to equivalent IFRS and adopt similar principles and treatment. As a result, the financial statements prepared under the new ASBE are more comparable with those prepared in accordance with IFRS than they would have been in the past. Overseas investors and users will understand the financial statements of Chinese enterprises better and the cost of re-preparing them when getting overseas listing will be reduced (Ernst & Young, 2006a). A list of the new ASBE is presented in Appendix A.

Ernst and Young (2006a) has analysed the key features and major changes of the new ASBE which are summarised in Table 1.

Although the new ASBE has fundamentally converged with IFRS, a few exceptions are still recognised in certain areas due to the unique circumstances in China. The key disparities (Ernst & Young, 2006a, 2006b) are summarised in Table 2.

4. Evidence on the actual harmonisation progress

Since issuing the ASBE in 1993, researchers have been attempting to prove that the Chinese standards have been catching up with their international counterparts. Studies documenting Chinese accounting reform have become available (Chen et al., 1997; Chen et al., 1999, 2002; Ding, 2000; Lin & Wang, 2001; Xiang, 1998). In order to evaluate the comparability and the compatibility of the Chinese standards,

Table 1
Key features of new Accounting Standards for Business Enterprises.

Key features	Relevant standards
Introduction of fair value measurement	ASBE Nos. 3, 11, 20, and 22
Introduction of accounting standards and detailed guidelines for business combinations and consolidated financial statements	ASBE Nos. 20 and 33
Previously off-balance-sheet items are now required to be recorded in the balance sheet	ASBE No. 22
Introduction of new standards for specialised industries (e.g. financial institutions, insurance companies, etc.)	ASBE Nos. 5, 10, 25, 26, and 27
Introduction of new standard on 'Impairment of Assets' specifying impairment loss cannot be reversed in future accounting periods.	ASBE No. 8
Introduction of stricter and more detailed disclosure requirements in line with IFRS	ASBE Nos. 28, 30, 34, 35, 36, and 37
Introduction of transitional provisions for first time adoption	ASBE No. 38

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