THE POSSIBLE APPLICATION OF INTERNATIONAL ACCOUNTING STANDARDS IN CHINA

by

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ABSTRACT

This thesis is a single case study on Chinese accounting, the research question it attempts to answer is the possible application of international accounting standards in China. In order to answer the research question, it first studies the differences of contexts between international accounting and Chinese accounting, subsequently, from the perspective of conceptual framework, elucidates the dissimilarities between Chinese accounting and international accounting and the causes which bring about these differences. The final conclusion is that China has not yet possessed the necessary conditions for the application of international accounting standards.

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List of abbreviations

Institutions

AAA	American Accounting Association
AICPA	American Institute of Certified Public Accountants
APB	Accounting Principles Board
ARB	Accounting Research Bulletin
ARC	Accounting Regulatory Committee
ARD	Accounting Regulatory Department (under the MOF)
ASB	Accounting Standards Board
ASBE	Accounting Standard for Business Enterprises
ASC	Accounting Standards Committee
CASC	China Accounting Standards Committee
CICPA	Chinese Institute of Certified Public Accountants
CPA	Certified Public Accountant
CPC	Communist Party of China
EFRAG	European Financial Reporting Advisory Group
EITF	Emerging Issues Task Force
EU	European Union
FAF	Financial Accounting Foundation
FASB	Financial Accounting Standards Board
FASC	Financial Accounting Standards Committee (AAA)
FEI	Financial Executives Institute
FRC	Financial Reporting Council
FRS	Financial Reporting Standard
GAAP	Generally Accepted Accounting Principles
IAS	International Accounting Standard
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
IFRS	International Financial Reporting Standard
IMA	Institute of Management Accountants
MOF	Ministry Of Finance (China)
SEC	Securities and Exchange Commission (the US)
SFAC	Statement of Financial Accounting Concept
SFAS	Statement of Financial Accounting Standard
SIC	Standing Interpretations Committee
SOE	State-Owned Enterprise
SOP	Statement Of Position
SSAP	Statement of Standard Accounting Practice
UITF	Urgent Issues Task Force

Technical

CCA	Current Cost Accounting
CoCoA	Continuously Contemporary Accounting
CVA	Current Value Accounting
FIFO	First-In, First-Out
LIFO	Last-In, First-Out

I INTRODUCTION

The idea for the study indicated by the title of this thesis originates from a press release by the International Accounting Standards Board (IASB) in 2005. That leaflet reads:

> **Bold steps toward convergence of**
> **Chinese accounting standards and international standards**
>
> Representatives of the China Accounting Standards Committee (CASC) of the People's Republic of China and the IASB met in Beijing…to discuss a range of issues relating to the convergence of Chinese accounting standards with International Financial Reporting Standards (IFRSs).
>
> At the conclusion of the meeting in November, the two delegations released a joint statement setting out key points of agreement, including the following
>
> - China stated that convergence is one of the fundamental goals of its standard setting programme.
> - China affirmed its intention that an enterprise applying Chinese accounting standards should produce financial statements that are the same as those of an enterprise that applies IFRSs.
> - The IASB delegation acknowledged that convergence to IFRSs will take time and how to converge with IFRSs is a matter for China to determine.
> - …China's Accounting Standards System for Business Enterprises is being developed with a view to achieving convergence of those standards with the equivalent IFRSs.
>
> (excerpted from IASB, 2005, bold type heading in the original)

In the following year, the Chinese Ministry of Finance (MOF) formally issued the Accounting Standards for Business Enterprises (ASBEs) which consist of a new Basic Standard (hereafter referred to as the '2006 Basic Standard') and 38 Specific Standards. The ASBEs cover nearly all of the topics under IFRSs and are substantially in line with them (summarised in Deloitte Touche Tohmatsu, 2006). Incidentally, what commands attention is that only does the MOF have the authority to promulgate accounting standards, whereas the aforementioned CASC is just an advisory body for setting standards under the control of the MOF, therefore all of the Chinese accounting standards and regulations cited in this thesis are issued by the MOF with the exception of the ones indicated separately.

Before the new ASBEs became mandatory for listed companies and were recommended to other enterprises from 1 January 2007, Chinese accounting practices had been regulated mostly by (a) the initial version of the *Accounting Standard for Business Enterprises: Basic Standard* (henceforward referred to as the '1992 Basic Standard', in comparison with the amended 2006 one under the same title), which was promulgated in 1992 and came into effect on 1 July 1993 to all enterprises, (b) some 30 unnumbered specific accounting standards, of which the first one came into force in 1997, and the scope of applications varied from covering only listed companies to all businesses, and (c) the year 2000 issued *Accounting System for Business Enterprises* (the '2000 System'), which functioned as a comprehensive and prescriptive uniform accounting system setting down a chart of accounts and detailed accounting entries, and was first applicable to equity joint ventures from 1 January 2001, then to all industries and firms later. In short, those precursory regulations were a mixture of accounting standards that drew heavily and largely on International Accounting Standards (IASs) published by the then International Accounting Standards Committee (IASC) and a uniform accounting system that kept to the rigid procedural accounting model, which was initially imported from the Soviet Union to support a central planning system (see Xiao et al., 2004[1]). Clearly, for the time being, accounting practices in China, at least those of listed companies, are governed solely by one set of accounting standards of IFRS style, namely the ASBEs.

1. ten relative instances

The convergence of Chinese accounting standards with IFRSs is indicated not only in form but also in the substance of accounting treatments. An example of illustrating this point could be the income taxes standard. A very general, to some extent highly debatable, background to accounting for deferred taxation is that in a large number of countries, including China, for a variety of reasons, accounting profit reported under generally accepted accounting principles (GAAP) differs from taxable profit calculated according to tax legislation. In other words, the amount of tax actually paid for a particular period often bears little relationship to the profit recognized in the income statement, and therefore

[1] That paper suggests that some articles of the 2000 System specify accounting principles, qualitative characteristics, definitions of elements of financial statements, and so forth; consequently, the 2000 System replaces the 1992 Basic Standard, which also has similar content. The actual practice was that the 1992 Basic Standard had never been invalidated owing to the implementation of the 2000 System; but inevitably, there was some overlap among multifarious regulations, which could be ambiguous in applications.

deferred tax is invented in view of the argument that the taxation charge should be matched against the accounting profit to which it relates, i.e. the accrual basis. Different approaches to deferred tax had been developed over the years. Under Chinese GAAP, the previous rules about income taxes were laid down in the 2000 System, which stipulates that an enterprise should adopt either the tax payable method or the tax effect accounting method to account for income taxes; enterprises that use the tax effect accounting method can adopt either the deferral method or the liability method for recognizing timing differences. To be specific, timing differences are defined as 'the differences between accounting profit before tax and taxable income due to different recognition periods for revenue, expenses and losses under tax rules and accounting requirements. Timing differences originate in one period and reverse in one or more subsequent periods' (Article 107 of the 2000 System). Under the tax payable method, also known as the flow-through method, an enterprise does not recognize the effect of timing differences, and the amount of tax expense is only the amount of tax payable relating to a period. Under both the deferral method and the liability method which is sometimes known as the income statement liability method, an enterprise recognizes the effect of timing differences, which will be deferred, known as making the deferred tax provision, and allocated, known as reversal, to subsequent periods. The pragmatic distinction between those two approaches to calculating the deferred tax liability is that the deferral method ignores the influence of changing tax rates on the timing differences that are recognized in earlier periods, and then any reversal of the effect on income tax in respect of timing differences is made at the original tax rate; conversely, the liability method requires the recalculation of the sum of accumulated timing differences at the current rate of tax to represent the potential liability, and any reversal is made at the current tax rate. In contrast to providing preparers with a free choice of the flow-through method, the deferral method, or the income statement liability method, the new standard ASBE 18 *Income Taxes* prohibits those aforesaid approaches to accounting for income taxes and mandates the balance sheet liability method to account for deferred tax on temporary differences at the current tax rate, in this place temporary differences are described as ‘differences between the carrying amount of an asset or liability and its tax base…’ (Chapter 3 of ASBE 18). The general principles of recognition, with some exceptions, are that a deferred tax liability should be recognized for all taxable temporary differences, and a deferred tax asset should be recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized (Chapter 4 of ASBE 18). In general, ASBE 18 converges with IAS 12 *Income Taxes*, which also permits exclusively the balance sheet liability method.

On occasion there is such a situation as that the ASBEs do not have absolutely corresponding IFRSs that deal with exactly the same topics, but for all that, the accounting procedures established under Chinese and IASB GAAP achieve their own convergence in practical terms. The debt restructuring standard could be a case in point. The primary version of *Debt Restructuring* standard was issued in 1998 and effective from 1999 onwards; subsequently, that standard was amended and the revised version became operative from 2001 until it was superseded by ASBE 12 *Debt Restructuring*. Article 2 of the earlier 2001 revised standard specifies that ‘a debt restructuring is an event in which the terms of a debt are modified as a result of a mutual agreement between a debtor and a creditor or a judgment by a court’; Articles 4 to 8 of that standard prescribe accounting by debtors, the main idea of which is as follows: the difference between the carrying amount of the debt to be restructured and the carrying amounts of the assets, or the face value of the equity interests, transferred to the creditor is recognized as capital surplus. In comparison with a broad definition cited above, ASBE 12 makes it clear that a debt restructuring is an event in which a debtor is in financial difficulty and a creditor grants a concession to the debtor in accordance with a mutual agreement or a court judgment

(Article 2 of ASBE 12). It could be argued that the clarification on identifying a debt restructuring event in ASBE 12, even the whole ASBE 12, employs the US standard issued by the Financial Accounting Standards Board (FASB), specifically Statement of Financial Accounting Standards (SFAS) 15 *Accounting by Debtors and Creditors for Troubled Debt Restructurings*, paragraph 2 of which states that a troubled debt restructuring occurs when the creditor, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that it would not otherwise consider. As to the recognition and measurement requirements, ASBE 12 sets down that the assets or equity interests received or surrendered by the debtor or the creditor are measured at fair values, as opposed to historical costs, and the resulting gains or losses are recognized in profit or loss instead of a non-distributable reserve account (Chapters 2 and 3 of ASBE 12). There is no corresponding international standard for ASBE 12, only relevant provisions are made in IAS 39 *Financial Instruments: Recognition and Measurement* under the 'derecognition of a financial liability' subheading. Principally speaking, as per paragraphs 40 and 41 of IAS 39, whether or not financial difficulty is the reason for the debt modification, the difference between the book value of a financial liability extinguished and the fair value of the consideration paid is recognized in current earnings. In effect, the accounting treatment for debt restructuring under ASBE 12 converges with the treatment according to IAS 39.

Some other examples of comparing the ASBEs with previous pronouncements on Chinese accounting and IASB GAAP are as follows: Article 17 of the original 2002 effective *Inventories* standard allows the use of the last-in, first-out (LIFO) method to determine the cost of inventories, in contrast, ASBE 1 *Inventories* proscribes the LIFO formula (Article 14 of ASBE 1). This change of disallowing LIFO, alongside the others, makes ASBE 1 consistent with IAS 2 *Inventories*. Under previous Chinese GAAP, by and large, in accounting for a non-monetary transaction, the cost of the received asset is recorded at the carrying amount of the asset surrendered (Article 114 of the 2000 System;

note: a *Non-Monetary Transactions* standard, which was first issued in 1999 and then revised in 2001, existed simultaneously with the 2000 System; in this instance stipulations in that revised standard and the 2000 System are identical); by contrast, although IASB GAAP does not contain one specific standard for all types of non-monetary transactions, IAS 16 *Property, Plant and Equipment* covers the general principle of non-monetary exchanges of tangible assets as follows: the cost of the asset involved is measured at fair value, providing the transaction has commercial substance, which means causing the cash flows of the entity to change (paragraphs 24 and 25 of IAS 16). Likewise, current Chinese standard ASBE 7 *Exchange of Non-monetary Assets* institutes the notion of commercial substance test, and requires that the measurement of non-monetary assets, including inventories, fixed assets, intangible assets and long-term equity investments, is based on the fair value unless the exchange transaction lacks commercial substance (Chapter 2 of ASBE 7). As a result of these amendments, the broad principles underlying ASBE 7 are the same as relevant international standards. One more case could be the accounting for convertible debts. In Chinese GAAP, Article 74 of the 2000 System stipulates that 'an enterprise should account for the convertible bonds issued in the same way as ordinary bonds before conversion is made…', however, ASBE 37 *Presentation of Financial Instruments*, Article 10 specifies that the issuer of a non-derivative financial instrument that has both liability and equity components should present those components separately in the balance sheet. Consequently, the recognition principle of convertible debts in ASBE 37 is equal to the one of IASB GAAP viz paragraph 28 of IAS 32 *Financial Instruments: Presentation*. In sum, the foregoing five examples illustrate a point that the adoption of the new ASBEs brought about Chinese standards substantial convergence with IFRSs.

Although there are still some differences between the ASBEs and IFRSs, the practical effects of some of those differences could be insignificant. For instance, in contrast with crediting the total amount of the grant to the capital reserve under former Chinese GAAP, ASBE 16 *Government Grants* requires that government grants related to assets, including non-monetary grants at fair value, should be presented as deferred income and recognized as income evenly over the useful life of the asset (Article 7 of ASBE 16). IASB GAAP in this area is provided in IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. In addition to the method adopted in ASBE 16, IAS 20 allows an alternative method for presentation in the balance sheet, whereby the grant is deducted from the carrying amount of the asset (paragraphs 24 to 27 of IAS 20). Although ASBE 16 does not permit a different approach to balance sheet presentation, both options have exactly the same effect on the operating results. Another situation is that the ASBEs may deal with issues which are not addressed in IASB GAAP, or vice versa. As an illustration, Article 5 of ASBE 20 *Business Combinations* explains that a business combination involving entities under common control is a business combination in which all of the combining entities are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory; moreover, ASBE 20 requires the use of the pooling of interests method for these types of business combinations (Chapter 2 of ASBE 20). In IASB GAAP, despite the fact that paragraph 10 of IFRS 3 *Business Combinations* gives an identical definition to the one just mentioned in ASBE 20, the accounting treatment for business combinations involving entities under common control is still not within the scope of IASB GAAP to date. This difference might be resolved by amendments to IFRS 3 in the future. In a similar way, IAS 29 *Financial Reporting in Hyperinflationary Economics* requires that the financial statements of an entity whose functional currency is the currency of a hyperinflationary economy should be adjusted to reflect year-end general price levels (paragraph 8 of IAS 29). As China is not a hyperinflationary economy, there is no ASBE equivalent of IAS 29. However, ASBE 19 *Foreign Currency Translation*, Article 13 specifies that prior to their translation, financial statements of a foreign operation which is operated in hyperinflationary economy should be restated in terms of general purchasing power. Obviously, this restate and translate approach is in line with IAS 29.

As for the remaining differences, it may be contended that the Chinese accounting standard setting unit and the IASB have been working together to reconcile some of the key differences. A typical case of this argument is that: Article 6 of ASBE 36 *Related Party Disclosures* states clearly that state-controlled entities should not be regarded as related parties simply because they are subject to control by the state. In contrast, this exemption for transactions between state-controlled entities is not given in the currently effective version of IAS 24 *Related Party Disclosures*. The recent development in this respect is that, in November 2009, following two earlier exposure drafts, the IASB published a revised version of IAS 24, of which the essential part is similar to the aforesaid provision in ASBE 36. Therefore, the difference in state-controlled entities will be eliminated when IAS 24 is formally applied from 2011. Finally, an example of important differences between Chinese and IASB GAAP could be the accounting for impairment losses. Article 17 of ASBE 8 *Impairment of Assets* strictly prohibits the reversal of all previously recognized impairment losses. Contrariwise, IAS 36 *Impairment of Assets* stipulates that '[a]n impairment loss recognized in prior periods for an asset other than goodwill shall be reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized' (paragraph 114 of IAS 36). A possible argument concerning this difference could be that, as specified by IAS 36, impairments should be reversed under defined conditions, but those conditions do not exist constantly, and therefore the influence of this dissimilarity between Chinese and IASB GAAP on accounting practices might be relatively unimportant.

In summary, the ten examples above cited could exhibit the current realities of Chinese accounting, mainly the fact that to the extent China's accounting standards have converged with international ones by now, in this aspect, the ten cases specifically evidence that under most circumstances, the ASBEs are in accordance with IFRSs, while under other circumstances, the number of differences between Chinese and international standards seems quite small, and the impact of those differences on accounting practices is conceivably limited. Or to cite the quotations from the leaflet on page 1, on the one hand, exactly as stated by the Chinese accounting officials, convergence is one of the fundamental goals of China's standard setting programme, this point could be illustrated both by the fact that the ASBEs have been developing with a view to achieving their convergence with the equivalent IFRSs, and by the fact that an enterprise applying the ASBEs could produce financial statements that are roughly the same as those of an enterprise that applies IFRSs; but on the other hand, certain divergence between Chinese and IASB GAAP is still existing in some areas, in addition, further convergence with IFRSs will take time and how to converge is a matter for the Chinese accounting standard setter to determine. As far as this thesis is concerned, it is hoped that the discussion in this thesis could be beneficial both to the knowledge of the status quo of Chinese accounting and to the prediction of its outlook, certainly, it should be pointed out that any viewpoint in this thesis is just a personal opinion of this writer.

2. the research question

From a historically developmental perspective, the writing of this thesis was not in the least possible twenty years ago, when even the debit and credit double entry bookkeeping technique had not been adopted by Chinese accounting, in contrast, nowadays the ASBEs are formulated targeting at their convergence with IFRSs. Now that the foregoing actualities have appeared, there seems to be some grounds to hope or to expect that the following situation is not unlikely to arise that apart from realizing convergence by the way of utilizing IFRSs to create national standards, as already chosen by the Chinese standard setter, another approach to convergence is the direct application of IFRSs. In terms of practical effects, whether or not to directly apply IFRSs into Chinese accounting does not make much difference as the specific accounting treatments and the finally presented financial statements prescribed in current Chinese and IASB GAAP are almost the same. Nevertheless, a direct application of IFRSs would generate some advantages, of which the obvious one is that when the IASB issues new standards, those changes could be immediately reflected in Chinese accounting accordingly. To take an example, ASBE 35 *Segment Reporting* provides that an enterprise should identify two sets of segments, viz business segments and geographical segments (Article 4 of ASBE 35); and prescribes that one set should be regarded as the primary segment and the other as the secondary segment, with considerably less information required to be disclosed for the secondary segment (Chapter 3 of ASBE 35). These stipulations in ASBE 35 are in agreement with the then valid IAS 14 *Segment Reporting,* but different from the new standard IFRS 8 *Operating Segments*, which replaced IAS 14 and came into effect from 2009. IFRS 8 abolishes the above-mentioned provisions and instead requires identification of an entity's operating segments on the basis of internal reports about components of the entity that are regularly reviewed by the chief operating decision maker in order to assess performance and to allocate resources. Consequently, a dissimilarity relating to accounting for segments of an enterprise appears between Chinese GAAP and IASB GAAP at the present time. Had international accounting standards been directly applied, this problem would have been avoided. Being able to keep consistent with IFRSs is only just one benefit, more importantly, one point claiming attention is that the present convergence of Chinese GAAP with IASB GAAP lies merely in specific accounting treatments, or to say, in provisions and stipulations (and may not be taken as genuine convergence), while the direct application of international standards may constitute a further step towards convergence to IFRSs (for the time being, there could be four expectations in the evolutionary convergence, namely, non-convergence, similarity in terms, a direct application and the genuine convergence). This thesis tries to explore the next step towards (genuine) convergence between Chinese and international accounting standards, that is, the possibility of a direct application of IFRSs (and at the same time, the possibility of genuine convergence), noticeably, any convergence could be affected both by the complexities of accounting concepts and by the complications in China's realities.

On the whole, this thesis aims to answer the question about the possible application of international accounting standards in China, which is also the title of this thesis, or more specifically, about what could be the reasons why international standards cannot be directly applied presently in China, and about what is the feasibility of fulfilling the direct application in the future. In order to answer the research question on the future of Chinese accounting, the logical order is supposed to be first discussing the current situation of Chinese accounting, specifically in three aspects, i.e. the 2006 Basic Standard, accounting measurement bases, and the accounting regulatory framework. Since the ASBEs are currently compulsory only for listed companies, the word 'application' in the research question means that international standards are directly applied to companies that adopt the ASBEs. International accounting standards in this thesis comprise IFRSs, IASs, Interpretations developed by the International Financial Reporting Interpretations Committee or the former Standing Interpretations Committee (SIC), and the 1989 published *Framework for the Preparation and Presentation of Financial Statements* (the 'IASB Framework'); the first three categories are normally termed as IFRSs or IASB GAAP. To sum up, the research question of this thesis is just its title, i.e. 'the possible application of international accounting standards in China', and its main body will be written out by means of unfolding layer upon layer, so readers probably could not get a complete conclusion until Chapter 6 and Chapter 8.

3. the research methodology

This thesis is a single case study on Chinese accounting. Yin (2009: 18) describes the scope of a case study as '[a] case study is an empirical inquiry that investigates a contemporary phenomenon in depth and within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident'. Yin (ibid: 8-10) points out that case study method is suitable for answering such kind of questions as 'how' and 'why' in relation to contemporary events, these questions are more explanatory. The object this thesis studies is primarily concerned with the harmonization of Chinese accounting standards with IASB GAAP, which is still an event in progress. This thesis is attempting to research how Chinese accounting probably harmonizes with the international one under the markedly different contexts of accounting standards' formulation and application between the two, this question belongs to the one of 'how' kind. Meanwhile, it is also trying to explore why Chinese accounting practices are dissimilar from the international accounting ones, this is a question of 'why' kind. Hence case study this thesis chooses is an appropriate research method.

Yin (ibid: 47-53) furnishes five rationale for single-case designs altogether, of which the one relating to this thesis is where the case represents an extreme case or a unique case. Evidently, The context and practices of Chinese accounting thoroughly differentiate from those countries which are adopting IFRSs, for example the European Union, this particularity could be helpful in understanding the requirements for the application of IFRS. In respect of the sources of evidence, this thesis utilizes the relative documentation, specifically, Chinese accounting standards. As for the aspect of analysing evidence for case study, the analytical technique this thesis makes use of is explanation building. Yin (ibid: 141) indicates that its purpose is to analyse the case study data by building an explanation about the case, he continues pointing out that '[t]o 'explain' a phenomenon is to stipulate a presumed set of causal links about it, or 'how' or 'why' something happened. The causal links may be complex and difficult to measure in any precise manner'. As far as this thesis is concerned, it is aiming at explaining which factors exerting influence on Chinese accounting through analysing accounting standards, these factors are hardly exactly worked out, if they could be grasped, they would facilitate making predictions for the development in future.

With regard to the subsequent arrangements of this thesis, Yin (ibid: 46) argues that all case study designs should involve the case itself and contextual conditions in relation to the 'case', although the boundaries between the case and the context are not likely to be sharp. Following the next chapter about literature review, chapter 3 will first discuss the contexts of international accounting and Chinese accounting, and the ensuing chapter 4 and chapter 5 will examine the dissimilarities between Chinese accounting and international accounting from the perspective of the contents and roles of conceptual frameworks. Chapter 6 will explore reasons why those differences have been caused, chapter 7 will relate to Chinese accounting profession and academics, and chapter 8 is the main conclusion of this thesis. The next chapter will review literature on Chinese accounting.

II LITERATURE REVIEW

Not many studies on the new ASBEs and the current Chinese accounting state of affairs had been published until the end of the year 2009. All the same, the analytical framework established by the previous literature should still be of great help in examining contemporary issues on Chinese accounting in the light of the fact that Chinese accounting development is in a continuous and evolutionary process. A special explanatory note about these arguments reproduced in this chapter is that they used to be advanced at particular times, but some of them are more likely to be inapplicable at present. The main purpose of citing them here is to facilitate the understanding of Chinese accounting from a historical angle.

1. Chinese accounting in the last 20 years

An important early book that systematically introduces accounting activities in China to international audience is *Accounting and Auditing in the People's Republic of China: a review of its practices, systems, education and developments*, which is a joint research study published in 1987 by Shanghai University of Finance and Economics and Centre for International Accounting Development, the University of Texas at Dallas. Chapter 1 'Introduction and Outline', written by Lou, a prominent accounting professor in China, gives the gist as follows:

> In looking at accounting as a discipline we tend to view it as having no national boundaries, in the sense that accounting principles and practices as they exist in different countries have much in common because they are the result of human wisdom and experience accumulated over centuries. However, we must acknowledge that accounting in many respects does have national or regional boundaries, in that the political, social and economic environment is bound to have far-reaching impact. Accounting may have to adapt itself to the political, social and economic peculiarities of each country, performing different functions and fulfilling somewhat different purposes which local conditions require.
>
> (Lou, 1987: 1)

And then that chapter amplifies such a particularity that China is a socialist country, in which a planned economy is one of the distinctive features of the socialist system (writer note: at that time). As theory and practice in accounting are determined by the purposes it serves in a particular economy, the practices and features of accounting in China are the end-products generated by the political, social and economic environment of China. Some highlights of the impact of these environmental factors on accounting in China are as follows: (a) Accounting theories are deeply rooted in the ideological foundation of Marxism-Leninism. Definitions of some basic accounting terms are directly linked to the notions elaborated in Marxist-Leninist political economics, for instance, fixed fund is defined as 'the fund used by enterprises as the means of labour'. (b) Uniform accounting system are enforced as a result of centralized control exercised over accounting affairs nationwide with the purpose of gathering consistent, comparable, and uniformly measured accounting data, which are closely coordinated with planning, financial and statistical measurements (Lou, 1987: 1-6). Chapter 2 'Financial Accounting and Reporting' (Wang and Qian, 1987: 9-29) studies the Chinese financial accounting system, which is a fund management oriented uniform accounting system. Fund is the monetary expression of property, goods and materials used in the process of the socialist production. The balance sheet is prepared on the principle of a specific fund for a specific purpose, and shows fund application on the one hand and fund source on the other. This paragraph manifests that, at the time of writing that book, the features of accounting in China were distinctly different from internationally accepted practices, owing to the fact that politics, especially the socialist ideology, pervaded the economy, inevitably, including accounting.

An essential book that reviews the accounting reform that brought international accounting practices to China is *Perspectives on Accounting and Finance in China*, which was edited by Blake and Gao, and published in 1995. Chapter 14 'The Trend of Accounting Reform in China: issues and environment' (Ren et al., 1995: 246-260) explores the influential factors in accounting reform in China. That paper postulates that accounting reform is the natural reaction to a changing socio-economic and political environment; and contends that the most significant factor in leading to accounting reform is the economic reform that transforms the economic structure from a socialist planned economy to a socialist market economy. However, that paper continues to declare that such changes in the economic environment could not happen without the Communist Party of China (CPC)'s focus moved from the ideological debate to economic development. Chapter 15 'Chinese Accounting Reform: reasons and effects' (Scapens and Hao, 1995: 261-284) emphasizes that the most important factor which influences accounting practices is possibly the country's economic system, that being so, Chinese accounting's developments depend on China's economic reform and openness to the outside world. Additionally, that paper traces an account of the history of setting the 1992 Basic Standard as follows: The speed of accounting reform was significantly accelerated by an important political event, namely remarks made by Deng Xiaoping on being bolder in undertaking reform during his tour of South China in the spring of 1992. At the start of working on accounting standards, the MOF's general line of thinking was that existing accounting practices should be changed gradually, and that accounting standards would be set up only when conditions had matured. Such thinking seemed too slow compared with the requirements for bolder reform. Following Deng's speech, the MOF hastened its steps towards accounting reform and issued the 1992 Basic Standard, along with 13 industry-based accounting systems, in December 1992.

Chapters 8, 9 and 10 by Liu and Eddie (1995: 139-158), Aiken et al. (1995: 159-177) and Xiao and Pan (1995: 178-199) respectively make an evaluation of the 1992 Basic Standard. The promulgation of the 1992 Basic Standard was a landmark for Chinese accounting reforms, principally contributed to the notable turnaround that international accounting standards and Western experience had begun to be used as a basis for developing Chinese accounting regulations. The 1992 Basic Standard, the main contents of which serve as a conceptual framework, incorporates four fundamental accounting assumptions, that is, accounting entity, going concern, accounting period and money measurement; institutes six accounting elements: assets, liabilities, owner's equity, revenue, expenses, profit and loss; adopts the new accounting equation Assets = Liabilities + Owner's Equity to replace the old one (Fund Applications = Fund Sources); defines such three major financial statements as balance sheet, income statement and statement of changes in financial position or cash flow statement; and also imposes the adoption of the debit-credit double entry bookkeeping method instead of the increase-decrease one. These changes have abandoned the fund-based accounting system and moved towards harmonizing Chinese accounting with international practices. But even so, the 1992 Basic Standard neglects many fundamental issues and lacks adequate discussion of a good number of equally important topics. Chapter 11 'A Comparison of International and Chinese Accounting Standards' (Liu and Turley, 1995: 200-226) demonstrates some important differences in terminology, classification and the accounting treatment of certain items between the Chinese accounting system and IASs, and judges that the new standards are still at the first stage towards accounting regulation which is implied in IASs and could be found in most Western countries. The main theme of the above two paragraphs could be that, in the early 1990s, by virtue of the gradual weakening of the ideological dominance, the socialist market economy was established to speed up economic development. In response to the new market-oriented economy and some decisive political factors (specifically, Deng's remarks during his southern tour), the MOF introduced an internationally accepted modern accounting system, but with many unique Chinese characteristics.

Xiang (1998) propounds that the recent economic reforms, particularly the enterprise reform in China, have fundamentally changed the corporate landscape, in view of the fact that the ownership structures of China's industrial and commercial enterprises are now highly diverse. In consistency with the dramatic economic changes, a number of accounting regulations were promulgated, and the enactment of 30 detailed accounting standards would ensue. The implementation of these accounting rules essentially transformed China's accounting from the traditionally rigid and uniform system into a predominantly Anglo-Saxon approach to financial reporting, and was a massive step closer to bringing China's accounting practices into conformity with IASs. Still, that paper accepts that China's accounting environment differs considerably from what is typically presumed by IAS, for example, the lack of independent and professional auditing makes the information provided under Chinese GAAP unreliable. Tang (2000), an influential figure of Chinese accounting, deems China's economic reform and increasing international exchange activities to be the main factors driving Chinese accounting towards internationalization. The remainder of that paper further develops some issues surrounding accounting standards setting, the accounting profession and accounting academics, and conveys the below views:

> Accounting practice, research, and education in China are in a period of rapid change. The general trend is from a planned-economy oriented, self-contained tradition toward an outward, open attitude. Internationalization is recognized as an appropriate route through which the level of accounting can be upgraded. Although recent experience shows that improvement has been great and fast, there is still long way to go.
>
> In accounting standards setting, it is probably right that we started with a general framework, however, it is hardly possible to be perfect without cumulated practical experience and the support from general education and research efforts. Gradual improvement is expected. In a country with a long history of planned economy, traditional thinking is deeply rooted, which could delay the acceptance of change by people concerned.
>
> The Chinese accounting profession is rather young. The education background of the majority of practitioners is insufficient and is difficult to change in a short time period. Professional ethics is a serious issue waiting to be dealt with. Real professionalism takes time to form.
>
> In the long run, through education and training, I believe it will be the academics who will play the most important role in upgrading the national standards of accounting practice.
>
> (Tang, 2000: 102)

Xiao et al. (2004) survey the coexistence of a uniform accounting system and accounting standards as well as the 2000 System. That article advances its ideas that, for one thing, the 2000 System brings China's accounting practices more closely into line with international ones, in particular, impairment losses in eight types of assets are required to be recognized; for another, political factors strongly influence the nature of the accounting system in

China. It observes in depth that the Chinese government, in part self-motivated and in part under external pressure, has been active in developing accounting standards in harmony with international accounting standards; however, it has retained a uniform accounting system in the 2000 System to accommodate the special circumstance of a transforming government, strong state-ownership, a weak accounting profession, a weak and imperfect equity market, and the inertial effect of accounting tradition and cultural factors. This paragraph could be summarized as follows: around the beginning of the 21st century, accounting in China has been moving towards internationalization, principally as a consequence of further economic reforms; however, as summed up by the title of Tang (2000)'s paper, the road to internationalization is bumpy, on top of that, politics still exert enormous influence on the accounting development in China.

2. environmental factors

It is commonly held that the development and practice of accounting are considerably governed by its environmental factors, and almost all of the above-stated literature verifies this point as well. More essays on this regard are quoted next. Winkle et al. (1994) advocate that a revision of Chinese accounting standards is essential for the success of privatization reforms, which include a share system of ownership, development of organized stock exchanges and listing of shares in Chinese companies on Western exchanges. Davidson et al. (1996) hold it that the following economic reforms have important impacts on China's accounting: the separation of ownership and management of enterprises, changes in the banking system since 1978 and the open-door policy. Consequently, the basic function of accounting information shifted from implementing macroeconomic planning and safeguarding national assets to decision making by enterprise management and external markets. Tang and Lau (2000) perceive the economic reform of state-owned enterprises (SOEs), the development of capital market and the increase in foreign direct investment as the three driving forces underlying the accounting changes dating from the 1992 accounting reforms. As a result, the pre-reform state controlled and tax driven financial reporting system has been gradually transformed into a capital market oriented system. Evidently, the above-mentioned literature shares a common view that the Chinese accounting reform is the outcome of its economic reform.

In the matter of cultural influence on Chinese accounting, Chow et al. (1995) applies the model (of culture) presented by Hofstede (1980, 1984, 1991; note: a second edition of the 1980 book that has merged the 1991 book was published in 2001) and Gray (1988) to make an analysis of Chinese societal values, and the basic conclusion of that paper is as follows: Firstly, Chinese society possesses the tradition of bureaucracy with a highly structured centralised administrative system, or to cite Hofstede's terminology, China is a society with large power distance, that means that people accept a hierarchical order in which everybody has a place, which needs no further justification. Secondly, the Chinese, especially under the influence of Confucianism and Marxism, credit a strong sense of obligation and responsibility to one's family and group as a virtue, moreover, an individual is expected to play a proper role under the kinship system rather than to develop one's own self; or to quote Hofstede's terms, Chinese society bears a property of collectivism, as opposed to individualism. Thirdly, the way the Chinese acquire knowledge relies heavily on reference to tradition and discourages the pursuit of original thought, in other words, Chinese society harbours high uncertainty avoidance, which Hofstede defines as the degree to which members of a society feel uncomfortable with uncertainty and ambiguity. Fourthly, Chinese society has a preference for modesty, quality of life rather than achievement in terms of material success, or in Hofstede's words, Chinese society shows less masculinity. Fifthly, Chinese society is long-term oriented, or to say, its culture values thrift and perseverance. (This writer would like to stress that the above description of the dimensions of Chinese culture stems from the views in Chow et al. (1995), and might not fully manifest the current situation in China.) Subsequently, on the basis of the above analysis of Chinese culture, that paper asserts that Chinese accounting is characterized by strong statutory control, high uniformity and a tendency towards conservatism and secrecy. van Hoepen (1995: 349-368) finds that Marxism, as the official ideology in China, is an important and inseparable part of modern Chinese culture. Since the CPC established the People's Republic of China in 1949, Marxism has significantly affected Chinese accounting, including accounting concepts and principles, the development of accounting as well as accountant's attitudes and behaviour.

On the subject of political influence on Chinese accounting, Gao (1995: 299-318) at first enumerates evidence of political influence throughout China's accounting education and accounting research, and at last comes to the conclusion that the CPC controls accounting researchers at both organizational and individual levels. Tang et al. (2003: 69-74) sketches out the following backdrop of how Chinese accounting standards have been settled: The MOF is empowered by the central government to administer nationwide accounting affairs. The Accounting Regulatory Department (ARD) of the MOF announces that itself is the official organization to develop accounting standards. According to the ARD, accounting standards in China are, and will continue to be, officially promulgated by the government, whereby being legally enforceable, and all business enterprises are required to comply with the standards. Xiao et al. (2004) disclose that direct government involvement in accounting regulation in China is a political tradition that originated in the era of central planning. During the process of moving to a market economy, the continuation of direct government involvement in accounting regulation is seen in the CASC, established in 1998 as a consultative body largely controlled by the MOF. One reason for (and perhaps also a consequence of) direct government involvement is that the accounting profession is politically weak. The professional body of auditors, the Chinese Institute of Certified Public Accountants (CICPA) is also under the control of the MOF. Against this background, the Chinese accounting regulators hold direct government involvement to be the only option, this is reflected in the following remarks made by one of the regulators when he recalled the debate at the end of the 1980s over who should set accounting standards: 'who should set them? Government or the private sector? Academics advocated a private standard setting body. But ask whether government will recognize accounting standards issued by a private body? If they are not acceptable by the government, what use will they have? …even the private sector would not accept accounting standards issued by a private body'. The above three paragraphs attempt to justify that the economic, political and cultural factors influence Chinese accounting development and system, more specifically, economic factors drive the accounting reform, at the same time, political factors dominate Chinese accounting system.

3. a summary

A tentative conclusion of the above analysis of the developments in Chinese accounting over the past 20 years could be that accounting practice in China converges with internationally accepted one by degrees, while many peculiarities remain; and the process of internationalization is influenced by environmental factors. Be that as it may, people may also take the following question into consideration: during the 20-year's accounting reform, as far as Chinese accounting is concerned, what have ever changed and what have never changed? It could be evident from the literature cited in this chapter that the specific accounting treatment changed somewhat, but the government-controlled accounting system has never changed. Coincidentally, this situation seems to vividly epitomize a notorious notion raised in the modern history of China (from mid-1800s to 1919), going as 'Chinese learning as basis and west learning for application'. The below quotation is an essay written by this writer specifically for this thesis:

The Westernization Movement and its theory 'Chinese learning as basis and west learning for application'

In the wake of the Arrow War began 1856 and ended in 1860, China became more fragile and weaker, and the Qing Dynasty was teetering on the verge of collapse. To be faced with such an acute situation, a group of the Qing bureaucrats reviewed the reason why China was defeated by the Western countries and found out it was their power and strength contributed to their possession of mighty armaments and advanced technology that surpassed China, so China should learn from the west countries in science and technologies to make China as powerful as Western countries. They championed a Westernization Movement in the latter half of 19th century in an attempt to prop up the precarious Qing Dynasty. During the Westernization Movement, Chinese students were sent abroad by the government, Western science and languages were studied, special schools teaching skills were opened in larger cities, arsenals, factories and shipyards were established according to Western models, advanced communication and transportation were introduced from west and so forth.

However, the leaders of the Westernization Movement raised and maintained a theory 'Chinese learning as basis and west learning for application' as their movement's banner and guiding principle all along. They insisted that Chinese learning, including China's three cardinal guides (i.e. ruler guides subject, father guides son and husband guides wife) and five constant virtues (i.e. benevolence, righteousness, propriety, wisdom and fidelity), the existing order and laws, especially the feudal social system, was the foundation of China's fate, and could never be changed and had to be kept intact. As far as Western learning concerned, only could Western science, technologies and some measures in education, taxation, military preparedness, laws, statute and the like be followed and applied. To the maximum, the west learning was a practical use aimed at strengthening the rule of Qing dynasty and it was a supplement to Chinese learning, by no means a replacement for it. Actually, at the later stage of the movement, many people demanded that China should introduce and apply the Western political system, including parliamentarian now that China had introduced and applied the Western science and technologies. Undoubtedly, those people could not be tolerated by China's ruler and were immediately suppressed.

Obviously, history has justified that the Westernization Movement and its theory 'Chinese learning as basis and west learning for application' are a farce and a total failure. Not only were the introduction and application of science and technologies inapplicable and impractical, but also the basis of the Qing dynasty was ultimately overthrown in 1911. Some techniques and skills cannot save a rotten dynasty without any radical and thorough political reforms or even revolution.

This chapter may infer such a concept of Chinese accounting: Chinese government-controlled accounting system [is taken] as basis and international accounting techniques [is taken] for application. (Or to put it another way, Chinese government politically takes the control of accounting system as an immutable foundation and pragmatically employs international accounting techniques for flexible applications.) In order to answer the research question, i.e. the possible application of international accounting standards in China, and to examine the impact of 'Chinese learning as basis and west learning for application' on the current Chinese GAAP, the next chapter will first make an comparison of contexts between IFRS and China.

III THE CONTEXTS OF INTERNATIONAL ACCOUNTING AND CHINESE ACCOUNTING

The research question of this thesis is primarily concerned with the possible application of international accounting standards in China. In logical order, to answer this research question should first examine the context in which both Chinese accounting standards and international standards have been formulated and applied, because different context could determine the dissimilarities between the two accounting systems and their possible convergence in future. There is one point needing an explanation that although this thesis uses the word 'accounting', strictly speaking, what it actually expounds is financial reporting, that is, furnishing users with financial accounting information. It is generally believed that financial reporting is one of vital elements in making corporate governance system effectively function, and corporate governance is an important enforcement mechanism for accounting standards (referring to Whittington, 1993). The first section of this chapter will begin with corporate governance to review the context of international accounting standards.

1. the context of international accounting

(1) corporate governance

Dating back to December 1992, the formal publication of the Cadbury Report became a milestone in corporate governance. In early 1990s, economic growth in the UK decelerated, some of companies with conspicuous success once shown in their published accounts were found to undertake fraudulent activities and ended up collapsing. To take three representative examples: one is that a boss of public companies (i.e. the Maxwell companies) with unfettered power gained from being both chairman and chief executive thieved pension funds from his companies to finance his other activities, subsequently his companies went bust, pensioners could not claim their company pension entitlement. The another one is that a private bank (that is, the Bank of Credit and Commerce International) was uncovered by financial regulators of several nations to have a lot of fraud and illicit dealings including money laundering, and finally was forced closure. The last one is that a company (namely Polly Peck) seemingly with healthy published accounts just the previous year was bankrupted the following year, and the company's boss was accused of false accounting and theft. (He was sentenced to imprisonment 20 years later). Scandals like these not only strongly attracted the UK's public and media attention but facilitated the speedy publication of the Cadbury Report. (The official title of the Cadbury Report is Report of the Committee on the Financial Aspects of Corporate Governance, and the chairman of the committee is Sir Adrian Cadbury, that is why this report is known as the Cadbury Report). The criticism of failure of corporate governance involves the one of auditing and accounting practices.

The significance of the system of corporate governance lies in the following grounds: Since the owners, principally the shareholders, delegate the running of a company to the management, 'agency problem' has arisen with the separation of ownership and control. On the assumption that the goals of the principal (owner) and agent (managers) conflict, agency problem specifically means the agents do not necessarily make decisions in the best interests of the principle, for instance, managers care more about maximizing their own perceived self-interest, instead of the maximization of long-term shareholder wealth. Under such circumstances, it is essential for principals to monitor agents, just as one definition of corporate governance indicates that 'the process of supervision and control intended to ensure that the company's management acts in accordance with the interests of shareholders' (Parkinson, 1995), or another definition in the Cadbury Report does that 'the system by which companies are directed and controlled'. The above brief introduction to corporate governance is derived from the agency theory; besides it, theoretical frameworks used to explain and analyze corporate governance also include transaction cost theory and stakeholder theory, all of the three theories are still in an ongoing development (referring to Solomon (2010: 3-25) for the introduction to corporate governance research).

The main areas covered in the Cadbury Report comprise the monitoring and assessment of the board of directors, the key roles of accounting and auditing functions in good corporate governance, the importance of institutional investors and so forth. And the more consequential is that the Cadbury Report adopts the 'comply or explain' approach for the UK corporate governance, which requires a company comply with a voluntary code of best practice, or the company should give an explanation if it does not comply with the code. Following the Cadbury report, other relevant reports have continued being published, primarily including: the Greenbury Report 1995 providing guidelines on directors' remuneration policy, the Turnbull Report 1999 presenting the framework for internal control, the Higgs Report 2003 producing recommendations for the role and effectiveness of non-executive directors, and so on.

In the current UK's regulatory framework for corporate governance, the Financial Reporting Council (FRC) is accountable for monitoring the operation of the corporate governance rules, and approving any changes to them. As for the FRC, it is the UK's independent regulator responsible for promoting high quality corporate governance and reporting to foster investment. It has overall responsibility for the regulation of accounting, auditing and actuarial profession; the UK's accounting standard setter (since 2012, it is known as the Accounting Council, but this thesis will not cover the standards formulated by it) referred to in this thesis is one of the FRC's subsidiaries (the above is shown on the website of the FRC). In history, the Hampel Report 1998 produced the Combined Code (1998) through having incorporated several reports previously published, subsequently the FRC reviewed the Combined Code several times. Originally, the Walker Report 2009 was aimed at reviewing the governance of banks and other financial industry entities, the FRC implemented some recommendations suggested in the Walker Report into its review of the Combined Code (2008), whereby bringing about the publication of the UK Corporate Governance Code (2010) and the UK Stewardship Code in relation to institutional investor activism (referring to PricewaterhouseCoopers LLP, 2010: 4001-4011; Solomon, 2010: 45-75 for the history and development of corporate governance in the UK).

The UK Corporate Governance Code (2010) continues adopting the 'comply or explain' approach. It is generally perceived that the advantages of this principles-based approach are that companies could decide the optimum corporate governance practice according to their own specific conditions and clearly explain to shareholders the reason for deviation. This flexibility encourages companies to comply in spirit rather than in letter. Incidentally, in contrast to the UK's corporate governance scheme is rules-based system typified by the US. To take an example, under the Sarbanes-Oxley Act of 2002, any corporate must abide by all of legal requirements, or else it would be considered as lawbreaking. To be more specific for financial reporting, the main principle stipulated by the UK Corporate Governance Code is that '[t]he board should present a balanced and understandable assessment of the company's position and prospects' (paragraph C.1). Whittington (1993, this paper relates to the problems of corporate governance around the publication of the Cadbury Report) contends that one of the major roles financial reporting plays in the corporate governance system is to furnish providers of finance, in a broader terms, including shareholders and lenders, with good financial accounting information in order that they could monitor directors' performance effectively (certainly, directors also need good management accounting information to carry out their monitoring and decision-making functions effectively). That said, improved financial reporting is only a necessary condition instead of a sufficient condition for effective corporate governance. The other necessary conditions in effective corporate governance system should embrace, for instance, external audit process so as to supply an independent check on the quality of financial reports, surely, also include all the other provisions contained in the UK Corporate Governance Code.

In respect of the interaction between corporate governance and financial reporting, Ball (2004, first version: 1996) uses a German corporate, Daimler-Benz listing on the New York Stock Exchange, as case study to carry out the relative research. There is one point needing attention that here mentioned circumstances arose at that time. The corporate governance of German companies is regulated by German company law, and like the UK, Germany adopts the ‘comply or explain’ approach too. One of the distinguishing features of the German governance structure is two-tier board system, consisting of a supervisory board and a management board. Specifically, all of the supervisory board members are nonexecutive, half of them are labour representatives elected by employees, the other half and a Chair by shareholders, such cases usually involve lending bank, (cross-shareholding) company, or government representatives; whereas the management board are comprised of only executives. The supervisory board oversees and appoints the management board, in addition, approves major business decisions. German banks are generally the dominant suppliers of equity capital, so it is easy to perceive that owners could better monitor managers under such system.

Since German corporate governance is an insider-dominated system, and Germany is a code-law country (the functions of capital market and legal system influencing corporate governance will be mentioned later), German corporates have incentives to reduce volatility in financial reporting. Those incentives primarily contain: for instance, managers’ performance is evaluated mostly by reported profits rather than share prices; employee bonuses is closely linked to reported earnings; tax considerations (under code law, income calculations for tax and financial reporting are almost identical) and so forth (for details referring to the summary of Ball, 2004). Unlike German corporate governance, the American one is an outsider-dominated system (the specific contents will be discussed later), and what it focuses is upon shareholder value, instead of stakeholders. Shareholders are in need of the transparency of information disclosure, for example, corporates need report losses in a timely fashion so as to facilitate shareholders' knowledge of whether managers' decisions have reduced shareholder value. Moreover, being dissimilar from German accounting rules, US GAAP has no enough flexibility to create hidden reserves. Hidden reserves means corporates make use of the methods, such as over-depreciation, creating 'provision for future losses' and so on to reduce earnings during better times, subsequently, draw on hidden reserves to cover losses or inflate earnings. Chiefly owing to timely loss recognition required by US GAAP, the ultimate result is Daimler's earnings under US GAAP is much more volatile than earnings under German accounting. From this case, it could be discerned that corporate governance has considerable impact on accounting practices, further, capital market exercises significant influence on corporate governance.

(2) capital market

The outside investors in capital market provide external financing for corporates. Because of business firms' purpose of obtaining capital, or putting in other words, investors' one of differentiating between 'good' and 'bad' business ideas and ensuring proportionate benefit from their investment, management has to communicate firm performance and governance to outside investors (to reduce information asymmetry and the agency problem). Corporate disclosure, mainly by means of regulated financial reports, is critical for the functioning of an efficient capital market. Amid the process, accounting standards, for example IASB GAAP, regulate the reporting choices available to managers in presenting the firm's financial statements (this paragraph is excerpted from Healy and Palepu, 2001).

It is commonly considered that the ways in which companies finance themselves and the structure of corporate ownership are the principal determinants of a country's corporate governance system. To take the above-mentioned as an instance, in respect of the classification of corporate governance, it could be categorized as outsider-dominated system represented by the UK and the US and insider-dominated system represented by Germany and some other countries; under the former, large firms are controlled by managers but owned predominantly by outside shareholders, and under the latter, firms are owned predominantly by insider shareholders who also wield control over management. It is needed to point out that the above classification is merely a rough one, and that does not mean corporate governance systems are necessarily categorized (this paragraph is extracted from Solomon, 2010: 194-198, for the comparison with different corporate governance systems, ibid.). Besides financial systems, legal systems have substantial influence upon corporate governance systems. La Porta et al. (1997) use a sample of 49 countries to research the link between legal environment, measured by both the character of legal rules and the quality of law enforcement, and the size and extent of a country's capital markets, including both equity and debt markets. Their examination finds that as for legal environment, in countries with lower level of investor protection, their capital markets are smaller and narrower, whereas countries with higher level of investor protection have bigger capital markets correspondingly. This is mainly because a good legal environment protects the potential financiers against expropriation by entrepreneurs, it raises their willingness to surrender funds in exchange for securities, and hence expands the scope of capital markets.

Returning to the relationship between capital market and corporate governance, it is generally deemed that transparency and timely information disclosure are major aspects of good corporate governance. Without this, investors would find it extremely difficult to value a firm, or assess the risk of its operations (see Hillier et al., 2010: 35). Barth and

Schipper (2008) define ‘transparency’ in a financial reporting context as the extent to which financial reports reveal an entity’s underlying economics in a way that is readily understandable by those using the financial reports. One concept which is closely connected with transparency is accountability, which has not yet had a precise definition, and whose basic meaning is that someone, for instance the management, is required to be responsible for their decisions. To take an instance, a set of financial statements is an important accountability document, moreover, action can be taken to make the directors preparing the financial statements liable for what are contained in financial statements (see Gray and Manson, 2011: 61-64). The quality of a firm’s disclosure could be assessed from the degree of transparency and accountability of the information to investors, the disclosures with higher quality could lower corporates’ cost of capital, hence it could be perceived that a well-developed capital market could finally reward or penalize a corporate’s governance practices and attitudes. As per this aspect, by exemplifying German public firms to carry out the research, Drobetz et al. (2004) finds a strong positive relationship between the quality of firm-level corporate governance and firm valuation.

The quality of corporate disclosure is decided by the development of capital market as well as by the standard of accounting profession. Auditors provide investors with independent assurance that the firm’s financial statements conform to GAAP. If auditors want to effectively enhance the credibility of financial statements, they have to be independent. Independent auditors are supposed to act in the interest of the firms’ investors (Surely they also could act in the interest of the managers that hire them. The detailed discussion on the topic of auditor independence could be referred to Healy and Palepu, 2001; Gray and Manson, 2011: 60-69). Furthermore, the protection for investors is mostly derived from laws and the effectiveness of their enforcement. La Porta et al. (2000) advocate the legal approach to corporate governance, just like the above-mentioned, the legal approach holds that the protection for outside investors should be afforded through the legal system. Strong investor protection is associated with effective corporate governance, and facilitates the development of financial market. It could be argued that whether corporate governance, capital market or accounting profession cannot be separated basically from the rule of law, for example, the legal liability of auditors also needs to be decided by the law.

(3) a brief summary

Viewing from the whole rather than from specificity, the above contents show that the context of the formulation and adoption of international accounting standards mainly includes the following factors: civil society with the rule of law, corporate governance with the ability of continually rectifying deficiencies, capital market enhancing transparency and accountability, independent accounting profession with high standard, and so forth; these factors make up an indivisible whole.

In respect of research methods, while Yin (2009: 46) points out that the design of case study is in need of an introduction to context, readers here could wait for the reading of the context until having looked through the whole situation of Chinese accounting discussed in this thesis. To do so possibly makes readers gain a better knowledge of the reasons why Chinese accounting peculiarities are existing and the possibility of the convergence of Chinese accounting with the international accounting in future. The next section will begin introducing the context of Chinese accounting with its history.

2. a brief history of Chinese accounting

(1) Chinese accounting before 1949

The literature review chapter in this thesis looks back on the history of Chinese accounting over the recent twenty years, and the following will review the history dating back to a longer time. The history of accounting in China can be traced to as early as more than 2000 years back and the evolution of the history has been symbolized chiefly by the gradual change in bookkeeping methods from single entry to double entry. Government accounting emerged during the Western Zhou Dynasty (from the 11th century BC to 771 BC), under the official who was in charge of the management of government properties, there was a comptroller general who was responsible for the collection of government revenue, control of expenditures, preparation for the state budget, and served other government accounting functions, such as financial reporting as ordered by the king. The government accounting used the input-output method of single entry bookkeeping (Fu, 1971; Gao and Handley-Schachler, 2003). In private sector, Chinese single entry bookkeeping slowly matured from the 7th to the 13th centuries and was widely used from the 14th century. This method was based on cash flows and the basic equation was Balance brought forward + New receipts - Amounts paid out = Balance in hand. From the late 14th century, an intermediate framework between single and double entry emerged and was called the Three Feet bookkeeping system, its main feature was double entry for non-cash transactions, while the single entry was for cash ones. In the middle of the 17th century, Longmen (literally 'dragon gate') bookkeeping system was created and employed by the salt producing industry in a specific region named Zigong, a city in Sichuan province in the south-western China. Under this method, every transaction was recorded as a dual entry. Longmen system provided the basis for the Four Feet bookkeeping system. From the 18th century, alongside the development of commodity economy, Chinese double entry bookkeeping system was gradually invented and called as the Four Feet bookkeeping system. The equation was Keeping = Owing +/- Profit or Loss. However, this system was only used in the limited industries and regions. Aiken and Lu (1998) point out that there are five significant differences between the Chinese and Italian styles of double entry bookkeeping: recording symbols, accounts classification, basic equation, recording principle and underlying theory, of which, the basic equation under the Chinese method was Keeping = Owing +/- Profit or Loss, while the one under the Italian style was Assets = Liabilities + Owner's equity. Those differences determine that it is impossible for the Four Feet system to evolve to the Western debit-credit style of double entry bookkeeping system. The modern Western accounting methods were introduced into China in the early 20th century and many accounting professionals advocated the use of Western accounting, but it was not universally welcomed (concerning the evolution of Chinese double entry bookkeeping, refer to Liu and Turley, 1995; Aiken and Lu, 1998). The evolution of Chinese accounting before 1949 was also influenced by Chinese cultural variables, e.g. Confucianism, feng shui and Buddhism (Gao and Handley-Schachler, 2003). In traditional Chinese philosophy, profit (Li) and justice (Yi) are diametrically opposed, and Confucius never talked about profit (at least in classical works of Confucian). That culture correspondingly resulted in discrimination against merchants and private accountants, whose activities were naturally categorized as profit (Li). For this reason, Confucianism could be deemed to have played a negative part in the development of Chinese private accounting (see Van Hoepen, 1995; Gao and Handley-Schachler, 2003).

(2) Chinese accounting from 1949 until 1979

The CPC established the People's Republic of China in 1949. As a Communist nation, China inevitably has some common characteristics of socialist politics and economy. In the aspect of politics, the fundamental institution in the power structure is the Communist party and the paramount power is concentrated in the hand of the Party's general secretary (or Mao Zedong, who was the chairman of the CPC), i.e. the Party's boss. The constitution asserts that the Communist Party is the leading force of the state; any utterance and actions against the Communist party must be severely prohibited and suppressed. The Communist party considers itself responsible for everything and has been taking a Big Brother role nationwide. The organization of the state and those who are working in the state apparatus are not allowed any autonomy at all. The structure of power is totalitarian in nature without checks and balances and independent courts. For example, nearly every appointment of the official on every rank is decided upon by the party instead of public election. Power and the official ideology are as inseparably linked as body and soul. Bureaucracy enjoys an almost full ideological monopoly. The official ideology is put forward by a vast apparatus of party, state, and mass organizations, served by the press, the other media, and educational, scientific, and cultural activity (Kornai, 1992: 34-39, 46-50). In the aspect of economy, politics still pervades the economy. The nominal owner of a firm is the state represented by the national government. According to official ideology, any industry is the property of the whole of the people. Planning features in the socialist economy, the national economic plan covers every aspect of the economy, its implementation is compulsory, and the quantitative targets are the most important of the plan's indicators, the intellectual forerunners of the socialist system regard that as one of socialism's great advantages. A firm is wholly dependent on the bodies above it, the important thing in its life and growth is not for the buyer to be content, but for the superior authorities to support it and help it out in time of trouble, in realities, there is no particular danger in running a loss, and equally, there is no particular advantage in making a profit. Even firms are going bust, the government would bail them out with a wide range of subsidization, including all kinds of grant, price support, negative taxation, and so on, all of the above have formed a very high proportion of the state's expenditure. The revenue generated by state-owned firms, including both the profits and the taxes and levies paid by firms, is the main entry on the revenue side of the budget. The major pricing principles are that prices must reflect the socially necessary costs and they ought to be stable. The prices are set and controlled centrally (Kornai, 1992: 71, 110-114, 125, 134-138, 145-151).

Accounting in socialist nations, including Chinese accounting, has many common hallmarks. In the market economy, the price system is the basis of an accounting system

(Stiglitz, 1994: 202). Bailey (1995) supports Stiglitz's argument and asserts that prices provide a guide for economically rational action and their quality on the market affects the quality of the information generated by the accounting system. Under socialism, prices are controlled and fixed by the central authorities and economic decisions are made by them on the basis of non-commercial criteria, usually political considerations; hence the data derived from the socialist accounting system lacks an economic content, in effect, accounting is neutralized and routinized, consequently it regresses to bookkeeping and is combined with statistical system (Bailey, 1988; 1995). As to the role of accounting in the socialist economy, it does not attempt to satisfy the information needs of users like in the market economy, but is used as a means for maintaining control over the activities of the SOEs in the central overseeing system (Bailey, 1988). In socialist accounting practice, there is a very rigid uniform rules-based accounting system under the administration of central control authority, which signifies that all the accounting rules are centrally devised and highly detailed, and cover all possible circumstances. All of the organizations are required to follow the rules strictly (see Jaruga, 1996). China, as a socialist nation, primarily followed the Soviet Union, which had dominated the socialist world, so it was characterized by Soviet Union's as well as the common features of socialism. In the economic sphere, centrally planned economy was introduced. All enterprises in China were either state or collectively owned. The whole national economy was controlled by the state, which not only determined everything for enterprises, but also covered their losses and took away their profits. Consistent with the economic system, China copied an accounting system that was based on the traditional Soviet material production system, which relied solely on physical quantities. Then the ARD under the MOF was established as the department to be in charge of accounting affairs and it commenced to enforce a uniform accounting system, which was a macro-oriented, industry-specific and fund-based system. The main purposes of that system were directed towards accountability and stewardship consistent with the needs of a planned economy, assisting in implementing state policy and the maintenance of state control over the means of production, and were aimed at the budgetary control of the appropriated resources, rather than the measurement of enterprises' operating performance and reporting of corporate financial condition, so the government became the exclusive user of external financial statements (relating to the establishment of Chinese accounting system after 1949, see Winkle et al., 1994; Aiken and Lu, 1998; Chan and Rotenberg, 1999; Huang and Ma, 2001: 13-29).

Apart from accounting system being grounded on the Soviet model rather than Western accounting, accounting in China suffered two major setbacks. The first one took place in the Great Leap Forward campaign. To put it crudely, the Great Leap Forward was launched by Mao Zedong, commenced in 1958 and ceased in 1960, and demanded to fulfill a high-speed economic development through a mass movement. It was characterized by four signals: first, high targets, which was typified by such breathtakingly surprising slogans as 'surpassing England within three years and catching up with America within five years', 'one Mu (equivalent to 0.16 acre) of land must produces five tonnes of wheat', and the like. All of the nation erected steels melting furnaces everywhere, even on Tiananmen Square, to achieve the target of eleven million and seven hundred thousand tonnes of steel in 1958 doubling the production in 1957, smoke spewed from the furnaces hung over China, ridiculously, owing to the bereft of, or thorough absence of any minerals and because of scares about the penalties for failing the targets, nearly everybody took almost all metallic objects, such as pans, children's toys, even handles and locks on the furniture, and so on, out of their home and put them into the furnaces, unfortunately, the steels melt by that primitive way were totally useless and just heaps of wastes. The second and third signals were respectively command at whim and wild exaggeration, the two could be clearly exhibited by the foregoing. The fourth one was 'going communist' trend, which was represented by the Rural People Commune Movement along with the Great

Leap Forward campaign. From 1958, the original systems of ownership in China's rural areas, including the individual ownership, private ownership, collective ownership, were all eliminated within less than one year, and all of farmers in China were forced to take part in the People Commune and had been known as 'member of commune' since then. In actualities, the People Commune is not only a form of economic organization, but also a level of government, subordinate to county government. According to Mao Zedong, the People Commune has two features: one is its huge size, which comprised 0.6 billion members at that time, and the other one is its equalization, which was once dubbed 'daguofan', i.e. to eat from the big rice-pot the same as everyone else literally in Chinese, and in effect, is indiscriminate egalitarianism. It is not hard to imagine that how farmers could do all they could in agricultural production now that they had been able to gain an equal share of income without doing the same amount of work as others else, or to say, they would certainly put the minimum energies and efforts instead of the maximum ones into that commune and get as many as possible from it. Inevitably, China's agricultural production from 1960 to 1962 sharply declined, especially the output of grains abruptly plummeted, a severe famine rapidly spread all over China, the more serious situation was that millions of people, mainly farmers starved to death. That led to the internal conflicts in the CPC and the Great Leap Forward campaign culminated in Mao Zedong's grudging and vague admission of his mistake, but that also put down the catastrophic root for the coming Cultural Revolution, which will be discussed next. The Great Leap Forward had a significant effect on Chinese accounting. To give an instance, from the Great Leap Forward viewpoint, the authorities considered that political and mass movements could be used to arouse the masses' enthusiasm, and the masses were the leading force for economic development, so any technologies, rules, laws, regulations, and so on should be simplified to be so plain that the masses could understand and master readily. In accordance with those requirements, the MOF introduced simplified rules and procedures for accounting systems and reporting. Nevertheless, under the influence of the then political climate, what actually occurred at the lower levels of government and in practice went far beyond the simplification of rules and procedures, in some parts of the country there existed little or no accounting procedures, that was greatly because wild exaggeration was one of the symbols of the Great Leap Forward and officials could be swiftly elevated by reporting highly inflated output and other exaggerated figures to their superiors, so the officials were bound to have an incentive to abolish financial controls and accounting system, which they thought of as barriers to their manipulating data. Furthermore, another instance happening in the Great Leap Forward was that from 1960, China advocated a policy of self-reliance caused by confrontation in the Sino-Soviet relationship (and accounting was required to be simple and easily understood by everyone), so Chinese accounting academics and practitioners created a specific Chinese accounting system with an emphasis on Chinese own pure socialist bookkeeping methods, because the debit-credit bookkeeping was capitalist and revisionist (indicates the Soviet Union) ideologically. The increase-decrease method was the most popular one and its basic equation was Total sources of funds = Total applications of funds and categories in the chart of accounts could be expressed mathematically as follows: Sources of funds + net increase or decrease in revenues = applications of funds + net increase or decrease in expenditures. Sources of funds referred to the channel for obtaining and generating funds, while applications of funds represented employment and utilization of fund in obtaining property, goods and raw materials for operation. The main financial statement was the fund-based balance sheet that emphasized the allocation of state resources to the entity rather than the reporting of the financial position of the entity (concerning the increase-decrease bookkeeping method, refer to Cheng, 1980; Aiken and Lu, 1998; Chan and Rotenberg, 1999; as for the history of Chinese accounting in the Great Leap Forward, see Huang and Ma, 2001: 30-39; Liu and Turley, 1995).

The second setback undergone by accounting in China happened in the Great Proletarian Cultural Revolution, or called as the Cultural Revolution, which lasted for up to ten years, from 1966 to the death of Mao Zedong in 1976, and convulsed the entire population. The Cultural Revolution was started by Mao Zedong, its main aim is generally considered to bring down his political rivals and thus restore his position as the supreme leader, which Mao thought to be threatened in the early 1960s. Mao and his key political allies pointedly directed the mass movement against the then Party apparatus and government bureaucracy and rendered them paralyzed. As a result of the chaos and violence brought about by the Cultural Revolution, China's economy suffered tremendously during this period. According to the assessment made by the CPC itself, at the end of the Cultural Revolution, China's economy was on the verge of collapse. During the 10-year period of the Cultural Revolution, '[a]ccountants and accounting teachers were exiled to the countryside to perform manual labour. Accounting education at university was almost completely stopped for about ten years.… Financial control mechanisms and accounting procedures were denounced as being inconsistent with and opposed to the revolution. In many organizations and enterprises, the revolutionary masses took over all accounting work and prepared accounting reports in whatever way they thought was appropriate for promoting the [Cultural Revolution]. Where accounting records were not kept, the practice of 'accounting without books' was not uncommon' (the above are extracted from Huang and Ma, 2001: 40-44). The history on the Cultural Revolution is too complicated, there are an enormous quantity of events and occurrences, and the resultant controversies and arguments, it is absolutely impossible even to simply list them in this chapter, so only to mention the bit of the above for the sake of the introduction to the then situation of Chinese accounting.

From the history of Chinese accounting before 1979 when economic reform was pushed through in China, it could be manifested that Chinese accounting is historically different from the Western accounting system, and in the contemporary era, particularly after the CPC took power in 1949, China's economy, including its accounting system, were nearly thoroughly isolated from the Western world, mainly owing to the political xenophobia. In addition, political factors began to predominantly control accounting from 1949 and made it highly politicized but insufficiently professionalized and theorized, let alone systematically academic research. Those disadvantages apparently widened the gap between Chinese accounting and international accounting in the past and would probably consume more time for their convergence in future.

(3) Chinese accounting after 1979

From 1979, the economic reform and open-door policy were adopted in China to rescue the economy and state power from the verge of collapse. As a result of the open-door policy, China has encouraged foreign investment by offering foreign investors more preferential treatments, such as exempt or lower taxation and cheaper land than towards domestic firms, and the amount of foreign investment mainly in the form of joint ventures in China has dramatically increased. However, the fund-based accounting system could not satisfy the needs of joint ventures, and the accounting information's foreign users, such as investors and accountants, could not understand Chinese financial statements, hence bringing about the barriers to communication and to decision making. That situation pressed Chinese accounting into changing it into internationally accepted practices. In response, the accounting regulations for joint ventures were issued by the MOF in 1985 (their full names are 'Accounting System of the People's Republic of China for Joint Ventures Using Chinese and Foreign Investment' and 'Chart of Accounts and Forms of Accounting Statements for Industrial Joint Ventures Using Chinese and Foreign Investment'; furthermore, besides being applicable to equity joint ventures, that accounting system could also be referred to by cooperative (or contractual) joint ventures and wholly foreign-owned ventures for their applying). Although it was just an accounting guideline for joint ventures, it was both the first time for the Western accounting practices to be introduced into China and the first attempt to harmonize Chinese accounting practices with international ones, in effect, the 1992 Basic Standard in general follows the model used for the regulations for joint ventures (in relation to joint ventures' influence on the reform of Chinese accounting, see Liu and Woodward, 1995; Shi, et al., 1995; Xiang, 1998; Blake et al., 2000). Moreover, Western management accounting practices were brought with joint ventures into China and could be transferred to Chinese enterprises (Firth, 1996). The introduction and development of management accounting in China also created a need for the reform of Chinese accounting system (Scapens and Hao, 1995). In a word, the huge increase in foreign direct investment led to the first step towards the adoption of internationally accepted accounting practices.

Another important aspect of the economic reforms is the restructuring of Chinese SOEs. The contract responsibility system was the first major reform model for SOEs from the early 1980s until 1995. Generally speaking, under this system, an enterprise would turn over a certain amount of its profits each year to the state during the course of the contract, the surplus profits were then at the company's disposal (and mainly be used for the purposes of investment, restructuring, and so on). As a result, enterprises seemed to have benefited from increased autonomy in investment and management and the economic efficiency was enhanced. However, another direct effect of this system was the short-termism, which meant managers solely concentrated on the quantitative targets laid down in the contract and sought short-term profit on the financial statements (accordingly, managers under the contract responsibility system preferred an accounting system that had a positive effect on reported profits) (Hassard et al., 1999). In spite of that, the reform of the SOEs provides a basis for China's accounting reform. For example, the recognition of the separate legal entity status of SOEs (prior to that, a SOE was deemed to be part of the state) enabled the entity concept to be introduced into Chinese accounting. Additionally, introducing the concept of going concern in the 1992 Basic Standard is the result of the reform that more and more SOEs are operating according to market conditions and unprofitable SOEs will inevitably go bankrupt. What matters more is that the reform of SOEs has made Chinese accounting system have to change its orientation from providing information used in state planning and control to providing information useful for management decision making. This change has important implications for financial reporting, since business financial statements must report assets, liabilities and owner's equity on the balance sheet and profit or loss on the income statement rather than fund balances and flows of allocated funds (relating to the effect produced by the reform of SOEs on Chinese accounting, see Davidson et al., 1996; Graham and Li, 1997; Tang and Lau, 2000). Some new information about the SOEs in China will be given in the next section.

The foundation of securities market is one of the leading aspects of China's economic reform. Shanghai Stock Exchange and Shenzhen Stock Exchange were officially established respectively in December 1990 and July 1991, following more than four decades of the suspension of securities business in China. In general, only a firm considered as having a good record and promising potential is allowed to be listed. At the beginning, the listed companies were only authorized to issue A shares to domestic investors, and in 1992, some companies, most of which had issued A shares, were authorized to issue B shares to overseas investors (the stipulation has been altered now, the next section will provide further information about that) to help China meet its need for foreign exchange. The establishment of the two stock exchanges fundamentally changed Chinese fund-based accounting system and drove it towards a capital market oriented system. Alongside the rapidly increasing number of the listed companies, high-quality financial information and especially the transparency rather than secrecy of the financial status of the listed companies are strongly demanded by more and more shareholders to facilitate their decision making. In response to the emerging stock market, a regulation on stock companies was issued jointly by the MOF and the State Commission for Economic Reforms and became effective in January 1992 (the full name of the regulation is 'Accounting System for Experimental Joint Stock Enterprises'; afterwards, the 1992 Basic Standard became effective, listed companies must follow both the 1992 Basic Standard and the regulation for stock companies; the regulation was amended in 1998 and supplemented by the 'Accounting System for Companies Limited by Shares: Chart of Accounts and Financial Statements'; subsequently the listed companies were required to implement the 2000 System up until 2007, since then they were requested to apply the ASBEs). The 1992 regulation for stock companies is the first regulation which adopts international practices for domestic enterprises and is in many respects similar to the accounting regulations for joint ventures issued in 1985 (in regard to the influence brought about by securities market on the reform of Chinese accounting, see Brayshaw and Teng, 1995; Chen et al., 1999; Tang, 2000; Chen et al., 2002). It could be noticeable that authorities attempted to tap the capital market to test the application of international accounting standards. The first facet was the application of specific accounting standards, which are similar to IASs. From 1997 to 1999, the MOF issued nine specific accounting standards, out of which there were seven being initially applied only to listed companies. The second facet was that the 1998 revised regulation for stock companies was issued specifically to eliminate discrepancies between the 1992 regulation and IASs. The third facet was that companies issuing B shares were required to prepare financial statements according to IASs for overseas investors (that requirement was amended at the end of 2009, and since 1 January 2010, those companies have been also able to adopt Chinese accounting standards) (see Chen et al., 1999; Chen et al., 2002). The unique feature that companies issuing B shares are required to publish financial statements in accordance with both Chinese accounting standards and IASs provides an opportunity to examine how accounting standards affect accounting earnings and the effects of harmonization of accounting standards. By analyzing accounting earnings based on Chinese accounting standards and IASs, Chen et al. (1999) find that the former is significantly higher than the latter owing to differences in accounting standards, opportunistic applications of Chinese accounting standards, and so on. Chen et al. (2002) show that the harmonization of accounting standards is not sufficient for the harmonization of accounting practice, due to a lack of quality auditing etc. Moreover, most listed companies in China have a substantial portion of government ownership. Sun et al. (2002) examine the relationship between the government ownership and the performance of listed companies, and then conclude that the relationship follows an inverted U-shape pattern. Too much government holding of SOE shares means too much control and interference in the economic operation of SOEs, whereas too little government holding means too little support from the government to pull the SOEs out of their difficulties. The next section will supply some pieces of the latest information about China's securities market.

To sum up, the foregoing brief description of the developmental history of Chinese accounting could demonstrate that having suffered several decades isolation (or several-century one if it is dated back to 1494, when Pacioli published his treatise) from international accounting, it is to meet the economic reform's need that Chinese accounting has started the process of its gradual convergence with international accounting, however, for the time being, that convergence seems to be merely within the scope of accounting treatments, the convergence in substance, especially in the concept of accounting apparently still has a long and zigzag way to go and much more time would be spent allowing for the historical and contemporary gap between Chinese accounting and international accounting, as the above shown. Chinese accounting regulators will continue to play a decisive role in the development of Chinese accounting in future, so the next section will examine what factors could affect their decision.

3. environmental influence on Chinese accounting

The below two essays are specially written by this writer for this thesis, the main contents of the first one relate to a personal observation of the SOEs and the securities market in China, and the second one refers to the political influence on Chinese accounting.

A short introduction to State-owned Enterprises and Securities Market in China

SOEs (namely state-owned enterprises) are one of the main China's characteristics, and also one of the relevant topics when China's economy, certainly including China's accounting, is discussed. Since the foundation of the People's Republic of China in 1949, China has altogether promulgated four Constitutions respectively in 1954, 1975, 1978 and 1982, and made four amendments to the 1982 Constitution (that is the current China's State Constitution) respectively in 1988, 1993, 1999 and 2004. All of the above Constitutions include the similar Articles as below (extracted from the (current) China's State Constitution): 'Article 6. The basis of the socialist economic system of the People's Republic of China is socialist public ownership of the means of production, namely, ownership by the whole people and collective ownership by the working people. The system of socialist public ownership supersedes the system of exploitation of man by man; it applies the principle of 'from each according to his ability, to each according to his work''. 'Article 7. The state economy is the sector of socialist economy under ownership by the whole people; it is the leading force in the national economy. The state ensures the consolidation and growth of the state economy.' until the 2004 amendment revises Article 11 of the China's State Constitution as follows: 'The state protects the lawful rights and interests of the non-public sectors of the economy such as the individual and private sectors of the economy. The state encourages, supports and guides the development of the non-public sectors of the economy and, in accordance with law, exercises supervision and control over the non-public sectors of the economy'. The SOEs in China are representative of Chinese economic system constitutionally announced and, to some extent, could reflect the transition of Chinese economic system from planned economy to socialist market economy and the change of the sector of economy from just taking the sector of socialist economy under ownership by the whole people as the leading force to also protecting the lawful rights and interests of the non-public sectors of the economy. From 1949 until 1979 when China began carrying out its policy of reform and opening to the world, nearly all of enterprises in China had been uniformly owned by the state, the other types of enterprises were mostly closed and foreign enterprises excluded from China especially during the Cultural Revolution (1966-1976) because they were considered to belong to exploitative class, bourgeois and capitalism. Since 1979, the above situation has changed so dramatically, multiple kinds of enterprises, including private enterprises, individual enterprises, joint ventures, foreign-owned enterprises, and so on, have swiftly appeared in China as well as SOEs and collective enterprises, as a result, the China's State Constitution has to be amended correspondingly. By and large, under any circumstance, SOEs have prominently featured in China's economy, and yet, in recent years, particularly, of late, they seem to show three alterations deserving of attention.

Firstly, the SOEs are becoming more monopolistic. Faced with the quick increase of various kinds of other enterprises, the scope of industries run by the SOEs has been fast changed from covering nearly every industry to selecting the most important ones mainly relating to the so-called 'national economy and people's livelihood', such as strategic resources, scarce resources, state secret or state security, and so on. More and more industrial giants have been established and centralized by the central government, the Premier of the State Council has become their immediate superior and actual boss. In tandem with the centralization, the monopolization of industry has been formed, fast-growing monopolistic barriers erected in an attempt to hinder competitors from entering SOEs' territory and to eliminate competition in the monopolized industries. In order to exemplify the fact, some representative cases are listed below, an extra attention may be needed paying to the word 'National' and 'China' in the names of these enterprises. All of internet, telephony and mobile business can only be handled by 'Big Three', namely, China Mobile, China Unicom, and China Telecom, if other enterprises intrude those business, slightly they would be fined a huge quantity of money, seriously their bosses and staff be put in prison according to the relative laws and rules mainly because this industry is concerned with state security. All of oil and gas business is operated by another ‘Big Three’: China National Petroleum Corporation, China Petroleum & Chemical Corporation, and China National Offshore Oil Corporation. All of railway transportation is solely and directly by the state rather than state-owned enterprise, i.e. the Ministry of Railway (which is dubbed ‘Railway Big Brother’). A considerable quantity of civic aviation business and banking business is handled respectively by another ‘Big Three’: Air China, China Eastern, and China Southern Airlines, and by ‘Big Four State-owned Banks’: Bank of China, Construction Bank of China, Industrial and Commercial Bank of China, and Agricultural Bank of China. In April 2003, the State-owned Assets Supervision and Administration Commission of the State Council was founded to specially manage and take care of 123 super SOEs (note: the latest figure) on behalf of the central government, besides the above mentioned ‘Big Three’, ‘Big Four’, such enterprises as below are included in the name list: China National Nuclear Corporation, China Aerospace Science and Technology Corporation, Aviation Industry Corporation of China, China State Shipbuilding Corporation, China Ocean Shipping Company, State Grip Corporation of China, China North Industrial Group Corporation, China South Industrial Corporation and so on (note: the names of the last two corporations are literally ‘China Weaponry Industrial Corporation’ and ‘China Weaponry and Equipment Corporation’ in Chinese, their English names are perhaps for the sake of secrete).

Second, the SOEs are more exclusively gaining profit. In planned economy, the SOEs were indifferent to profit, because whatever gain or loss, the income of their staff still kept the same, but now, the income are tightly pegged to profit. So it is understandable for them to take gaining the most profit as their ultimate goal. However, their profits are mostly dependent on their monopolistic position instead of their own competitive abilities, hence known as ‘monopolistic profit’ (which is easy money indeed). For example, China’s most population of more than 1.3 billion in the world provides the above mentioned ‘Big Three’ of the telecommunications industry with an enviably gargantuan market: there are 1.11 billion, 0.8 billion and 0.115 billion users of telephony, mobile phone and internet respectively (the figures are from the publication by the Ministry of Industry and Information Technology on 22 July 2010). It is not hard to imagine that such a market is bound to generate astronomical profits. Nevertheless, in spite of those profits, the ‘Big Three’ are still discontented and harness their monopolistic price and charge to grab extra profit. (There is a notorious dual-charge for mobile phone calls, that is, the receiver has to pay for each received call at 30%-50% of calling charge, regardless of constant and bitter complaints from millions of users, this problem remains unsolved for dozen years mainly because of the government’s acquiescence as well as the monopoly of ‘Big Three’, the users have to accept the unreasonable price charged by ‘Big Three’, unless they will never use mobile phone in China. In fact, a great deal of foreign companies hope to run mobile phone business in China promising to charge much less than China’s ‘Big Three’, but they are rejected by Chinese government. The monopolistic profits make the staff of the monopolistic SOEs and their families enjoy a high standard of living by gaining enormous income which is much higher than ordinary people’s income and usually several times and even more than tenfold.) This kind of monopolistic income is too unfair and leads to increasingly stronger grudge against the CPC (i.e. the Communist Party of China, the ruling party) and the government, and becomes a factor causing social unrest and a (tough) problem for the CPC and the government. In reality, most of profits gained by the SOEs are taken away by the central government for their investments and expenditures, so the government has to be financially and economically dependent on the SOEs, for a reward, it offers the SOEs a great numbers of privileges, such as cheaper lands, favourable loans, easier way to banks’ credits, diverse fiscal funds and so on. Another important and effective way for the government to support the SOEs financially is to help them to be listed both on domestic and global stock exchanges, in another words, nearly all of the SOEs which are running monopolized industries and business are listed companies, and the values of their shares have made up most proportions of Chinese stock market. Furthermore, there is a phenomenon constituting attention, the SOEs are attempting to monopolize nearly every lucrative industry (for example, on-line games have enjoyed a vast market in China and generated immense profits, the CPC and the government are contemplating to bring it into the scope of business of the SOEs through so called ‘combining three nets (namely, internet, telephony net and television net) into one’).

Third, the SOEs are becoming more politicized. In recent years, the CPC has strengthened their supervision and control over the SOEs, predominantly by control over their executives. For example, Hu Jintao underlines that ‘we (i.e. the CPC) will advance reform of the personnel system in [SOEs] and public institutions and improve management of executives suited to conditions in these enterprises’ (see his Report at the Seventeenth National Congress of the CPC, below called as Hu Jintao’s Report). The chairman of the board of directors (usually is also the secretary (i.e. the head) of the Leading Party Members’ Group of an enterprise), chief executive officer, chief finance officer, general engineer and other high-rank management of all of the SOEs subordinated to the central government must be selected and appointed by the Central Committee of the CPC and are granted ministerial or quasi-ministerial rank, that means all of the largest SOEs in China are directly managed and controlled by the Central Committee of the CPC. Certainly, management must take literally carrying out the Party's instructions and being in line with the Party's spirits as top priorities on their agenda and tends to subordinate consumers' and individual investors' interests and requirements to the Party's. Noticeably, Chinese SOEs possess the properties of a political party and serve both for economy and politics.

From the above introduction to and analysis of China's SOEs, a conclusion could be drawn that China's SOEs both determines China's economy and features in Chinese securities market, and at the same time, China's economy determines China's accounting and China's securities market features in China's accounting, therefore Chinese SOEs could be one of important guiding forces for the reform and development of Chinese accounting and one of necessary references for the accounting standard setter. The above description of Chinese SOEs seem somewhat lengthy, but Chinese SOEs bear some of China's characteristics which sounds a bit strange to the ones in other countries, and a brief introduction to Chinese SOEs could provides a beneficial background to Chinese accounting.

With respect to the securities market, the history of China's securities market can be traced back to the 1860s connecting with the Westernization Movement. From that time until the early 1950s, there had unremittingly been securities transactions and exchange institutions in Beijing, Tianjin, Shanghai and several other large cities in China. After the foundation of the People's Republic of China in 1949, securities were considered belonging to capitalism and stock trading were defined as activities of illegally gaining money, and no doubt they were quickly prohibited and cancelled. Since 1952, when the last securities exchange was closed in Tianjin, China's securities business and the relative institutions had thoroughly vanished for exact 38 years under increasingly arch-left thoughts and consecutive political movements.

In the early 1980s, the minimal quantities of securities transactions began emerging along with the introduction of reform and opening up policy. However, they confronted intense pressures and sharp criticisms from the so-called orthodox ideology, of which the most typical is 'securities is named after capitalism instead of socialism' and hardly stopped halfway.

Crucially thanks to Deng Xiaoping's compromise by putting forward his suggestion of temporarily taking securities business as a tentative trial and then deciding on continuing or ceasing it depending on the result. Afterwards, securities' popularity with more and more investors proved the experiment successful. Since 1990s, in tandem with further reform and opening to the world and quick development of economy, securities have been unexpectedly booming. At the end of 1991, the Shanghai Stock Exchange and the Shenzhen Stock Exchange were both established, 1947 companies and 2868 securities in total have been listed on them by now, and 140.7684 million accounts of investment have been opened with them by 15 January 2010, and of which the effective accounts are 119.703 million according to the figures provided by the Shanghai and Shenzhen Stock Exchanges. On the basis of the above number, excluding institutional investors, a rough estimate believes the number of individual investors should be over 50 million at least or to somewhere around 70 million, equivalent to the British population. (These individual investors are known as 'gumin' in Chinese, literally meaning 'stock people'. This situation is exaggeratedly described as 'all of nation is trading stocks', and there is a humorous jingle that '1.3 billion Chinese people, 1 billion have become 'stock people', the remaining 0.3 billion people, hastening to become 'stock people''.) In October 1992, the Securities Committee of the State Council was founded, and in 1998, it was integrated into the China Securities Regulatory Commission. In December 1998, the Law of the People's Republic of China on Securities were published and taken into effect.

China's stocks are divided into A share and B share, the former can be purchased only by the Chinese residence and Qualified Foreign Institutional Investors (QFII) in Renminbi, and the latter, at the early stage, only by foreigners, but now, also by the Chinese residence, in US dollar in the Shanghai Stock Exchange and in Hong Kong dollar in the Shenzhen Stock Exchange. There are some Chinese companies which are registered in mainland China and listed in Hong Kong, Singapore and in the US, and this type of stocks are known as H share (named after the first letter of Hong Kong), S share (first letter of Singapore) and N share (first letter of the NYSE, NASDAQ) respectively. The companies listed in Hong Kong, that is H share, was once required to apply international standards, but from 1 January 2010, that requirement was cancelled, instead, ASBEs are allowed to use (however, the investment in Singapore, the US, and other countries, must use the standards locally required).

At the very beginning, China's securities market is so negligible in the size of business and in the number of investors that the setter of accounting standards hardly paid any attention to it, not to mention consideration of meeting investors' needs for information. Nevertheless, the dramatic development of securities business and swift increase of investors was far beyond the accounting standard setter's imagination and expectation, and have outgrown the creation of accounting standards for a long time. Facing such a huge population of investors, especially individual investors, if their interests cannot be guaranteed but be violated, that will directly harm millions of investors and families financially and easily cause social unrest, this situation is indeed not in accordance with the principle of 'putting people first as its core and overall consideration as its fundamental approach' taken as the staple of Scientific Outlook on Development presented by Hu Jintao, the incumbent head of the Party and the state (see below for further explanation of Scientific Outlook on Development). Additionally, China continues stressing to 'expand opening up in scope and depth and improve [its economy]' and 'adhering to the basic state policy of opening up' and 'will better integrate [its] 'bring in and go global' strategies, expand the areas of opening up…' (see Hu Jintao's Report). For instance, a growing number of Chinese enterprises have been accelerating their listing on international stock markets in recent years. The foregoing demonstrates that the big change and development of securities business have become a direct driving force for the setter of Chinese accounting standards to contemplate on how to make the accounting standards to catch up with the pace of investment both on domestic and international securities markets, since accounting information is an indispensable tool for securities business.

The Communist Party of China and Accounting

As opposed to most of countries in the world, Chinese accounting standards are drawn up directly by the MOF (i.e. the Ministry of Finance), one cabinet of the central government. Moreover, nearly all of the standard setters are government officials appointed by the CPC (namely the Communist Party of China), the ruling party, and the vast majority of them are members of the CPC. It is apparent from the above facts that the creation of accounting standards in China is highly political. Therefore, a brief introduction to China's history, not least its modern history and contemporary era, and to the CPC's history, is vital to the exploration of any possible convergence of Chinese accounting standards with international standards, that is also the central topic of this thesis.

a brief introduction to Chinese history

Historians usually take the period from 1840 (the outbreak of the Opium War) to 1919 (the May Fourth Movement) as China's modern history and the one from 1919 up to now as the contemporary era. The Constitution of the People's Republic of China (called as the China's State Constitution below) carries out the following valuation of the two histories from the very first sentence of its Preamble: 'China is one of the countries with the longest histories in the world. The people of all nationalities in China have jointly created a splendid culture and have a glorious revolutionary tradition. Feudal China was gradually reduced after 1840 to a semi-colonial and semi-feudal country. The Chinese people waged wave upon wave of heroic struggles for national independence and liberation and for democracy and freedom. Great and earth-shaking historical changes have taken place in China in the 20th century. The Revolution of 1911, led by Dr Sun Yat-sen, abolished the feudal monarchy and gave birth to the Republic of China. But the Chinese people had yet to fulfill their historical task of overthrowing imperialism and feudalism. After waging hard, protracted and tortuous struggles, armed and otherwise, the Chinese people of all nationalities led by the [CPC] with Chairman Mao Zedong as its leader ultimately, in 1949, overthrew the rule of imperialism, feudalism and bureaucrat capitalism, won the great victory of the new-democratic revolution and founded the People's Republic of China. Thereupon the Chinese people took state power into their own hands and became masters of the country'. 'After the founding of the People's Republic, the transition of Chinese society from a new-democratic to a socialist society was effected step by step. The socialist transformation of the private ownership of the means of production was completed, the system of exploitation of man by man eliminated and the socialist system established. The people's democratic dictatorship led by the working class and based on the alliance of workers and peasants, which is in essence the dictatorship of the proletariat, has been consolidated and developed. The Chinese people and the Chinese People's Liberation Army have thwarted aggression, sabotage and armed provocations by imperialists and hegemonists, safeguarded China's national independence and security and strengthened its national defence. Major successes have been achieved in economic development. An independent and fairly comprehensive socialist system of industry has in the main been established. There has been a marked increase in agricultural production. Significant progress has been made in educational, scientific, cultural and other undertakings, and socialist ideological education has yielded noteworthy results. The living standards of the people have improved considerably'.

And then the China's State Constitution summarizes the history of contemporary era and lays out the tasks and outlook for the future of China: 'Both the victory of China's new-democratic revolution and the successes of its socialist cause have been achieved by the Chinese people of all nationalities under the leadership of the [CPC] and the guidance of Marxism-Leninism and Mao Zedong Thought, and by upholding truth, correcting errors and overcoming numerous difficulties and hardships'. 'China will be in the primary stage of socialism for a long time to come. The basic task of the nation is to concentrate its effort on socialist modernization along the road of Chinese-style socialism' (note: 'Chinese-style socialism' was earlier translated into 'socialism with Chinese characteristics'). In particular, the China's State Constitution affirms that 'under the leadership of the [CPC] and the guidance of Marxism-Leninism, Mao Zedong Thought, Deng Xiaoping Theory and the important thought of Three Represents, the Chinese people of all nationalities will continue to adhere to the people's democratic dictatorship and the socialist road, persevere in reform and opening to the outside world, steadily improve socialist institutions, develop the socialist market economy, develop socialist democracy, improve the socialist legal system and work hard and self-reliantly to modernize the country's industry, agriculture, national defence and science and technology step by step and promote the coordinated development of the material, political and spiritual civilizations, to turn China into a socialist country that is prosperous, powerful, democratic and culturally advanced'.

There are three points deserving of attention. The first one is that nearly the whole of the Preamble of the China's State Constitution is quoted above without any abridgement, the intention of doing so is to present the original material for a comparison between the China's State Constitution and the Constitution of the CPC below cited, and to reveal such a fact that the spirit of the state is identical with the Party's spirit and their political principles are grounded on the same thing. The second one is that the above citations seem somewhat lengthy, but could be necessary and beneficial for obtaining a general idea of China's yesterday, today and tomorrow through understanding what the country's rulers or governors are thinking, are doing and are planning (at least on paper), as they can nearly entirely determine China's destinies. And the third one is that the history is most easily offended and easily controversial, and view of points about history are innumerable and diverse, but this thesis is just about accounting, and will not and cannot involve itself into debates about China's history. Hence, at this place, what could be done only is selecting Chinese official descriptions and opinions about its history, although the official history could bear unavoidable subjectivity, prejudice, and even untruth. In addition, to do so can make it clear what the historical conceptions of the Chinese leaders are (as documented), and further, what their conceptions of governing power are, that may help understand why there is a conceptual gap between China's accounting and the international one.

a short introduction to the CPC

In Article 1 of its Chapter 1 'General Principles', the China's State Constitution proclaims that 'The People's Republic of China is a socialist state under the people's democratic dictatorship led by the working class and based on the alliance of workers and peasants'. As for the question of who is the working class, the Constitution of the CPC declares in its General Program that 'The [CPC] is the vanguard both of the Chinese working class and of the Chinese people and the Chinese nation. It is the core of leadership for the cause of Chinese-style socialism…'.

The CPC was founded on 1 July 1921 (according to the official description). The General Program of the Constitution of the CPC announces that 'the [CPC] takes Marxism-Leninism, Mao Zedong Thought, Deng Xiaoping Theory and the important thought of Three Represents as its guide to action', the following ideological terminologies are all extracted from the General Program of the Constitution of the CPC, and they claim attention that they only convey the opinions of the CPC. As for Marxism-Leninism, the Constitution of the CPC makes such an evaluation: it 'brings to light the laws governing the development of the history of human society. Its basic tenets are correct and have tremendous vitality'. 'So long as the Chinese Communists uphold the basic tenets of Marxism-Leninism and follow the road suited to China's specific conditions and chosen by the Chinese people of their own accord, the socialist cause in China will be crowned with final victory'.

The CPC have undergone four generations of leaders in its history. The first one is Mao Zedong, whom and whose thought (i.e. Mao Zedong Thought) the Constitution of the CPC assesses as follows: 'The Chinese Communists, with Comrade Mao Zedong as their chief representative, created Mao Zedong Thought by integrating the basic tenets of Marxism-Leninism with the concrete practice of the Chinese revolution. Mao Zedong Thought is Marxism-Leninism applied and developed in China; it consists of a body of theoretical principles concerning the revolution and construction in China and a summary of experience therein, both of which have been proved correct by practice; and it represents the crystallized, collective wisdom of the [CPC]. Under the guidance of Mao Zedong Thought, the [CPC] led the people of all ethnic groups in the country in their prolonged revolutionary struggle against imperialism, feudalism and bureaucrat-capitalism, winning victory in the new-democratic revolution and founding the People's Republic of China, a people's democratic dictatorship. After the founding of the People's Republic of China, it led them in carrying out socialist transformation successfully, completing the transition from New Democracy to socialism, establishing the basic system of socialism and developing socialism economically, politically and culturally'.

The second one is Deng Xiaoping, whom and whose theory (i.e. Deng Xiaoping Theory) are judged by the Constitution of the CPC to be that: 'After The Third Plenary Session of the Eleventh Party Central Committee (note: December 1978), the Chinese Communists, with Comrade Deng Xiaoping as their chief representative, analyzed their experience, both positive and negative, gained since the founding of the People's Republic, emancipated their minds, sought truth from facts, shifted the focus of the work of the whole Party onto economic development and carried out reform and opening to the outside world, ushering in a new era of development in the cause of socialism, gradually formulating the line, principles and policies concerning the building of Chinese-style socialism and expounding the basic questions concerning the building, consolidation and development of socialism in China, and thus creating Deng Xiaoping Theory. Deng Xiaoping Theory is the outcome of the integration of the basic tenets Marxism-Leninism with the practice of contemporary China and the features of the times, a continuation and development of Mao Zedong Thought under new historical conditions; it represents a new stage of development of Marxism in China, it is Marxism of contemporary China and it is the crystallized, collective wisdom of the [CPC]. It is guiding the socialist modernization of China from victory to victory'.

The third one is Jiang Zemin, whom and whose theory (the important thought of Three Represents) the Constitution of the CPC makes its appraisal of as follows: 'After the Fourth Plenary Session of the Thirteenth Party Central Committee (note: June 1989) and in the practice of building Chinese-style socialism, the Chinese Communists, with Comrade Jiang Zemin as their chief representative, acquired a deeper understanding of what socialism is, how to build it and what kind of a party to build and how to build it, accumulated new valuable experience in running the Party and state and formed the important thought of Three Represents (note: the formal statement of this theory is that the Party must always represent the requirements of the development of China's advanced productive forces, the orientation of the development of China's advanced culture, and the fundamental interests of the overwhelming majority of the people in China, and the above is extracted from Jiang Zemin's Report at the Sixteenth National Congress of the CPC in November 2002). The important thought of Three Represents is a continuation and development of Marxism-Leninism, Mao Zedong Thought and Deng Xiaoping Theory; it reflects new requirements for the work of the Party and state arising from the developments and changes in China and other parts of the world today; it serves as a powerful theoretical weapon for strengthening and improving Party building and for promoting self-improvement and development of socialism in China; and it is the crystallized, collective wisdom of the [CPC]. It is a guiding ideology that the Party must uphold for a long time to come. Persistent implementation of the Three Represents is the foundation for building the Party, the cornerstone for its governance and the source of its strength'.

The fourth one is Hu Jintao, the incumbent head of the state and the Party, whom and whose theory (the Scientific Outlook on Development, note: which could be likewise translated into the Scientific Development Concept) the Constitution of the CPC makes the following description of: 'Since the Sixteenth National Congress [of the CPC] (note: November 2002), the Central Committee of the Party has followed the guidance of Deng Xiaoping Theory and the important thought of Three Represents and, by pooling the wisdom of the whole Party to meet new requirements of development, formulated the Scientific Outlook on Development, which puts people first and calls for comprehensive, balanced and sustainable development. The Outlook is a scientific theory that is in the same line as Marxism-Leninism, Mao Zedong Thought, Deng Xiaoping Theory and the important thought of Three Represents and keeps up with the times. It is an important guiding principle for China's economic and social development and a major strategic thought that must be upheld and applied in developing Chinese-style socialism'. Hu Jintao detailed his Scientific Outlook on Development in his Report at the Seventeenth National Congress of the CPC in October 2007 (below called as Hu Jintao's Report) that the Outlook 'takes development as its essence, putting people first as its core, comprehensive, balanced and sustainable development as its basic requirement, and overall consideration as its fundamental approach'.

The aim of writing down so many words to enumerate the changes of CPC's leaders and their theories is totally for the understanding of the political and historical backdrop to the evolution and outlook of Chinese accounting, because China is indeed with its characteristics, which is similar to nearly none in the other parts of the world and is featured by the CPC's political ideology exerting powerful influence on every aspect, every profession, every undertaking, every individual and so on, no doubt covering the setting of accounting standards. For example, the CPC ideology's pervasive propaganda, repeated inculcation and protracted instilling have made it insinuate into accounting setters' thoughts, and have presumably resulted in both the accounting setters perceptibly, or in most circumstances, imperceptibly signifying the Party's spirit in the process of setting standards, taking the

Party's requirements as the basis for their final decision about what can be accepted and what must be rejected, and the accounting standards inevitably bearing the hallmark of the Party's ideology more or less, let alone the enormous impact created by the Party's overwhelming political power, which will be discussed next.

This essay cites three documents at length, that is Hu Jintao's Report, the Constitution of the CPC, and the China's State Constitution, all of which are the most formal and authoritative presentation of the CPC's political ideology at the present time and in unison squarely reiterate upholding Four Cardinal Principles, namely, to keep to the socialist road and to uphold the people's democratic dictatorship, leadership by the Communist Party, and Marxism-Leninism and Mao Zedong Thought. The Four Cardinal Principles are both a strict political limit which must not be gone beyond in contemporary China and a sensitive barometer of whether the CPC will change course. Despite that, if a careful comparison is made, some subtle differences between the description of the Party's guiding theory in those documents will be revealed, for instance, the Party's doctrine of Marxism-Leninism has somewhat changed from original Marxism-Leninism to 'Marxism-Leninism applied and developed in China' (referred to Mao Zedong Thought), to 'Marxism of contemporary China' (referred to Deng Xiaoping Theory), to 'a continuation and development of Marxism-Leninism, Mao Zedong Thought and Deng Xiaoping Theory' (referred to Jiang Zemin's the important thought of Three Represents), to being 'in the same line as Marxism-Leninism, Mao Zedong Thought, Deng Xiaoping Theory and the important thought of Three Represents' (referred to Hu Jintao's Scientific Outlook on Development); from the literally complete Marxism-Leninism to the integration of its tenets with China. That seems as if a shade of looseness emerged from something which used to be very strict and never unchangeable. To go further into the current social realities in China, if the gradual alterations and growing diversity of people's life style, ideology, moral values and so on are taken into consideration, a conclusion could be drawn that the CPC's current policies, especially the one of reform and opening to the outside world, have become increasingly pragmatic and flexible albeit it still upholding orthodox ideology, and even a bold expectation could be held that a direct application of international accounting standards in China is in some likelihood in the near future.

the CPC and China's accounting

The question of why there is a relation between a political party and a country's accounting standards is rare in the other countries of the world. However, it is true of China's actualities, to have a conception of that could be helpful in analyzing the trends towards convergence between Chinese accounting and international accounting. By and large, it is useful to elucidate the four aspects below to show the tightness of the connection between the CPC and the Chinese accounting standard setter.

Firstly, the precise setters of China's accounting standards are the No. 1 and No. 2 divisions of the ARD (namely the Accounting Regulatory Department), the ARD is a division of the MOF, and the MOF are directly subordinate to the central government, i.e. the State Council. The Constitution of the CPC stipulates in Article 46 of Chapter 9 'Leading Party Members' Groups' that 'a leading Party Members' Group may be formed in the leading body of a central or local state organ, people's organization, economic or cultural institution or other non-Party unit. The group plays the role of the core of leadership. Its main tasks are to see to it that the Party's line, principles and policies are implemented, to discuss and decide on matters of major importance in its unit, to do well in cadre management, to rally the non-Party cadres and the masses in fulfilling the tasks assigned by the Party and the state and to guide the work of the Party organization of the unit and those directly under it'. It is very clear from the above citation that the CPC take tight control of the leading bodies including the MOF, namely the ones with gargantuan power, through the Leading Party Members' Group. (Mao Zedong has a known saying that 'In the east, the west, the north, the south and the middle, among the party, the government, the army, the civilian and the students, it is the Party that leads everything'.) Apart from what China's State Constitution and the Constitution of the CPC have openly announced, there is another fact that the Central Commission of the CPC, according to different fields, has founded several so-called 'leader small groups' (which could also be translated into leadership small groups), which are directly under the Standing Committee of the Political Bureau of the CPC, the paramount leader group in China, and headed by its members (note: there are nine members in total and they are the top such as Hu Jintao, the General Secretary of the Central Committee of the CPC and the President of the People's Republic of China, Wen Jiabao, the Premier). In reality, these groups control the routine works of the central government. For example, the leader small group for finance and economy includes the heads of National Development and Reform Committee, the MOF, the People's Bank of China, China Insurance Regulatory Commission, China Securities Regulatory Commission, State-owned Assets Supervision and Administration Commission of State Council and so on, and Wen Jiabao, the Premier, is its head, and the other two vice premiers are the assistant heads. It supervises prominent economical and financial activities in micro-scope, and decides on the important policies in macro-scope, concretely controls the ministries and commissions subordinate to it, including the recommendation about the appointment of their heads. Major issues such as the reform of Chinese accounting system ought to go through its discussion and approval. Additionally, among others, there is a Central Commission for Politics and Law, which leads and controls the Ministry of Public Security, the Supreme People's Court, the Supreme People's Procuratorate, the Ministry of Justice and so on. Evidently, the CPC, leads, governs, controls China's administration, legislation and judiciary in effect. The increased tightness and roughness of the control on the state powers by the CPC has a considerable connection with the Collapse of the Soviet Union, the Revolutions of Eastern Europe, and certain political event, all of which have given the CPC a grove lesson on how to maintain its running of the state and not to lose their power. Nevertheless, every industry, every trade, every business, every undertaking has its own specific feature, which should be paid special attention; every profession, every science, every field has its professional peculiarities and is often faced with particular problems, which demands relative experts to address and tackle scientifically and discreetly. It is unimaginable that politicians can be more familiar with accounting than accountants and that they can think of professional issues such as how to introduce international accounting standards to deal with problems arising from foreign investment in the same way as investors, lenders and so forth.

Secondly, the CPC is always 'adhering to the principle that the Party is in charge of cadre management', and 'will establish a scientific mechanism for selecting and appointing cadres…' and must 'enforce stricter oversight over the whole process of selecting and appointing cadres' (see part 10 of Hu Jintao's Report). The Constitution of the CPC highlights that 'the Party attaches great importance to education, training, selection and assessment of cadres…' (Article 33 of Chapter 6 of the Constitution of the CPC). The cadres indicated here are a substitute for officials, which sounds a little disapproving owing to its being reminiscent of mandarins in the old times. In practice, the appointments of ministers of every ministry are decided by the Political Bureau and the Standing Committee of the Political Bureau of the Central Committee of the CPC and announced via the National People's Congress. The heads of inferior departments and provisions are appointed by the Leading Party Members' Groups of ministries. The way above described is the single route for anyone to become the official of the government. Besides 'the principle that the Party is in charge of cadre management', the CPC also adheres 'to the principle of the Party being in charge of personnel' and 'will make plans for training all types of personnel with the focus on high-level and highly skilled ones' (part 10 of Hu Jintao's Report). To take an example, at universities in China, the presidents of universities at first class such as Peking University and Tsinghua University are appointed by the Central Committee of the CPC and granted a vice ministerial rank; the ones of universities at second class by the Leading Party Members' Group of the Ministry of Education and a rank of departmental rank (at the same rank as the ARD); and the ones of universities at normal by the provincial committee of the CPC and a departmental or quasi-departmental rank. The heads of faculties are appointed by the university committee of the CPC and granted a vice departmental or divisional rank. The professors are appointed by the university committee of the CPC and usually put on the rank of division or quasi-division. In China, official ranks weighs much more than academic or professional level, because it can bring you more material comforts, such as higher salary, more academic funds (and better medical treatment, better quality housing and at the same time, considerable spiritual contentment, such as admiration from others and self-regarding superiority in society, and so on; so more and more teachers and professors at universities have been doing their best to gain a higher official rank, instead of researching and teaching). In addition, universities are mostly funded directly by the state, namely indirectly by the Party. The Party has given admitting intellectuals to the Party a priority, if you are a professor, or an excellent student, or a high-level professional, the Party is very likely to persuade you into applying to join the Party.

Thirdly, the majority of the officials of the government are members of the CPC, the higher the level of the office, the higher the proportion of members of the CPC, for example, most (nearly 95 percent) of the officials in the ministries of the central government are members of the CPC, that means most of the setters of China's accounting standards belong to the CPC, even those who are non-Party members have affiliated themselves with the CPC, otherwise, they cannot attain and retain their posts in such an important and powerful institution. (At present, in all ministries in China, only the ministers of the Ministry of Public Health and the Ministry of Science and Technology are non-Party cadres, while the first vice ministers of the two ministries are (and must be) members of the CPC and the heads of the Leading Party Members' Groups, and at the ministerial rank.) Now that a person has become a member of the CPC, the person 'must conscientiously act within the bounds of Party discipline' (Article 37, Chapter 7 of the Constitution of the CPC). According to the Constitution of the CPC and other relative documents, the discipline is very stringent, for instance, 'When, on behalf of the Party organization, an individual Party member is to express views on major issues beyond the scope of the existing decisions of the Party organization, the content must be referred to the Party organization for prior discussion and decision, or referred to the next higher Party organization for instructions. No Party member, whatever his or her position, is allowed to make decision on major issues on his or her own. In an emergency, when a decision by an individual is unavoidable, the matter must be reported to the Party organization immediately afterwards. No leader is allowed to take decision arbitrarily or to place himself or herself above the Party organization' (Article 16 of Chapter 2 of the Constitution of the CPC). 'Party members must firmly uphold the centralized and unified leadership of the Party, conscientiously abide by the Party's political discipline, always be in agreement with the Central Committee and resolutely safeguard its authority to ensure that its resolutions and decisions are carried out effectively' (part 10 of Hu Jintao's Report). Any members who violate the Party's discipline will be taken 'five measures: warning, serious warning, removal from Party posts, probation within the Party, and expulsion from the Party' 'depending on the nature and seriousness of their mistakes'. To be worse, they are very likely to be fired from their job post (which provides them with much more incomes than mass of ordinary people, including periodically increased salary, a wide variety of bonus, allowance and things of that description, medical care nearly fully paid by state, and even free apartment, if you have been working in the government institutions such as the MOF). Evidently, the setters of Chinese accounting standards cannot and dare not express their own opinions freely, in particular on 'the major issues', let alone objections to their leaders' view of points, proposals or decisions.

Fourthly, Hu Jintao, in his Report, repeats stressing that 'to stand in the forefront of the times and lead the people in opening up new prospects for the development of the cause, the Party must improve itself in a spirit of reform and innovation and stay as the firm core of leadership for this cause', 'To achieve the main objectives of strengthening the Party's governance capability', 'better grasp the laws concerning the Communist Party's governance', 'improve the leading bodies' art of leadership and governance capability' and so on. From the foregoing quotations, it is noticeable that to retain the CPC's governance of the state has always been a priority on the CPC's agenda, all it has done is completely subject to this objective, which, certainly, is the guiding line that the setting of accounting standards must follow and the most prominent interests that all of accounting activities in China must ensure. Under such circumstances, it is very hard or impossible for the accounting standard setters to give full consideration to the requirements of users of accounting information and to serve users' interests (in reality, the users are inclined to be the victims of violations of rules and laws, and such unfortunate cases abound in China and have become increasingly rampant).

Marxism mentioned in the above essay is one of the guiding principles of the CPC, and materialist dialectics is a key component of Marxism, the possible connections between Marxist dialectics and accounting will be generally mentioned below (why to write this section is because Chinese accounting standard setters are inevitably affected by Marxist philosophy more or less). Materialist dialectics was given systematic form by Engels; three Engels' dialectical laws comprise the interpenetration of opposites, the transformation of quantity into quality, and the negation of the negation. Engels defines the first law as 'the two poles of an antithesis, like positive and negative, are just as inseparable from each other as they are opposed, and despite all their opposition they mutually penetrate each other' (Anti-Dühring, Introduction). To take an example of accounting, the two qualitative characteristics, i.e. relevance and reliability (referred to on page 28 and 29) could only be traded off, but not be fully satisfied simultaneously, or the one is removed and the other one retained. The 2008 Conceptual Framework Exposure Draft suggests that two fundamental qualitative characteristics should be relevance and faithful representation (mentioned on page 32 and 33), in effect, whatever wording is used, both of them must be contradiction of opposites, put it in other way, accounting information cannot have only one fundamental characteristic, therefore any statement is contentious. The tenor of the second law, i.e. quantity and quality law, is that qualitative (differences that cannot be expressed merely in figure are qualitative) changes are brought about only by quantitative increases or decreases. To exemplify accounting, owing to a gradual increase in the use of fair value in IASB GAAP, the IASB commences a project on reporting financial performance, the essence of the project is to replace the income statement with a layered matrix structure in order to show the effects of unrealized revaluation changes, that is, of remeasurements at fair value (see Barker, 2004; Alexander and Archer, 2007: 1.12-1.14 for further details). The instance could manifest that the increasing adoption of the quantitative aspect of the fair value could lead to a qualitative change of preparing a new financial statement (surely, in this instance, using that new type of statement as a substitute for the current income statement is fairly impossible for the time being; furthermore, the application of the new financial statement could drive more items to be measured at fair value). The gist of the third law, i.e. the negation of the negation law, is that there is an evolution in the form of a spiral: the negation of a system is negated to produce another system that is in some important respects a repetition of the first, but on a higher level. To give an example happening in the UK, in order to cope with changing prices (mainly in relation to inflation; particularly in the 1970s and 1980s, the very high rates of inflation pose a considerable challenge to the traditional historical cost based accounting system), having undergone many years of debate on inflation accounting, the UK standard setter of that time, the ASC, issued SSAP 16 *Current Cost Accounting* in 1980. Broadly speaking, SSAP 16 requires listed and other large companies to publish CCA accounts together with historical cost accounts (companies have the option to choose either of the two as their main financial statements). At first, SSAP 16 achieved very high compliance rates; and yet, owing to a decline in the rate of inflation and a related change in the fiscal and monetary policies towards inflation carried out by the UK new government taking office in 1979, in addition, because of some serious technical weaknesses existing in SSAP 16 itself, in the subsequent years, the compliance rates sharply declined (from 95 percent in 1981 to 6 percent in 1985), and SSAP 16 ceased to be a mandatory standard in 1985. It could be thought of that the primary historical cost system is negated by the CCA system (brought about by SSAP 16), which in turn is negated by the withdrawal of SSAP 16, amid that process, people deepen their understanding of the price change accounting system (the above contents concerning Marxist dialectics are from Kolakowski, 1978, reprinted in 2005: 308-326; as for SSAP 16, referring to Tweedie and Whittington, 1984: 106-151; 1997).

4. a brief summary

From the examination of the history of Chinese accounting and the introduction to the economic and political factors which have impact on Chinese accounting, it could be viewed that China has no the elements in IFRS context. First of all, China is not a country with rule of law, and does not devote much attention to the idea that capital market should enhance transparency and accountability, corporate governance is bereft of enforcement mechanism for accounting practices. Under such difference of context, the next chapter will begin the study on the substance of Chinese accounting and international accounting with conceptual framework.

IV A DISCUSSION OF CONCEPTUAL FRAMEWORKS

There has not yet been a universally accepted answer to the question of what a conceptual framework for financial accounting and reporting is to date. One of the early official interpretations is given by the FASB in Statement of Financial Accounting Concepts (SFAC) 2 *Qualitative Characteristics of Accounting Information* issued in 1980 as follows: 'The conceptual framework is a coherent system of interrelated objectives and fundamentals that is expected to lead to consistent standards and that prescribes the nature, function, and limits of financial accounting and reporting' (page 8 of SFAC 2). Some observations on the FASB's above definition are that: The second attributive clause 'that prescribes the nature, function, and limits of financial accounting and reporting' is pertinent to the subject matter of a conceptual framework, which is a prescriptive set of guidelines. SFAC 5 *Recognition and Measurement in Financial Statements of Business Enterprises*, issued in 1984, could be a counterexample of this point, since that statement only describes five different measurement attributes in practice and suggests that the application of different attributes will continue (paragraphs 66-70 of SFAC 5) (Solomons, 1986). As regards the first attributive clause 'that is expected to lead to consistent standards', it could be noticed that alternative formulae to measure the cost of inventories inevitably causes inconsistency in the inventory standard (Accounting Research Bulletin (ARB) 43, Chapter 4 *Inventory Pricing*); furthermore, none of those alternatives is consistent with, for example, the accounting for available-for-sale securities, which are required to be carried at fair value on the balance sheet (SFAS 115 *Accounting for Certain Investments in Debt and Equity Securities*; besides, SFAS 115 itself is not consistent either) (see Rosenfield, 2006: 406 and 407). Since those two are restrictive relative clauses, the adjective 'coherent' may also be in doubt as a consequence. As for the other adjective 'interrelated', SFAC 2 does not clarify how relevance and reliability are interrelated rather than contradictory to each other (Macve, 1981, in 1997: 77). Had the components that are questionable been deleted the FASB's definition could have become as follows: the conceptual framework is a system of objectives and fundamentals.

The word 'theory' is defined as 'a system of ideas or statements explaining something…' on page 3236 of Shorter Oxford English Dictionary published in 2002. On this account, it is reasonable to argue that the conceptual framework attempts to be an accounting theory even if it may not meet the criteria established by itself. It looks fairly feasible that any individual with relevant intelligence could develop an accounting theory that has similar elements to a conceptual framework. Compared to official conceptual frameworks, those individual works could be possibly more coherent academically and more inexpensive financially (see Macve, 1983a, in 1997: 170-178). Even though they can provide a basis for official conceptual frameworks such as Solomons (1989, reprinted in 1997), none of those individual studies is or is called a conceptual framework. This implies that there is a special reason for the existence of conceptual frameworks. Some quotations from conceptual frameworks developed by different standard setters are given below: 'The [FAS]Board itself is likely to be the most direct beneficiary of the guidance provided by the Statements in this series. They will guide the [FAS]Board in developing accounting and reporting standards by providing the [FAS]Board with a common foundation and basic reasoning on which to consider merits of alternatives' (page 8 of SFAC 2). 'The purpose of the Framework is to: (a) assist the Board of IASC in the development of future International Accounting Standards and in its review of existing International Accounting Standards…' (paragraph 1 of the IASB Framework). 'The primary purpose of articulating such principles is to provide a coherent frame of reference to be used by the [AS]Board in the development and review of accounting standards…' (paragraph 2 of the *Statement of Principles for Financial Reporting* (UKSP) issued by the Accounting Standards Board (ASB) of the UK in 1999). Perceptibly, all of the aforementioned documents confirm that the primary purpose of conceptual frameworks is to aid standard setters in developing accounting standards on a consistent basis, which could also be the primary reason for the search for a conceptual framework. Further, conceptual frameworks guide accounting standards setting, and accounting standards are the finished product from accounting standards setting, therefore conceptual frameworks underpin accounting standards (cf. Schipper, 2003). Alternatively, the premise and the conclusion in the last sentence could be written as passive voice: the standards setting process is guided by conceptual frameworks, and accounting standards are underpinned by conceptual frameworks. However, neither of the two claims is not controversial (e.g. Dopuch and Sunder, 1980; Nobes, 2005). The above two paragraphs discuss page 8 of SFAC 2, paragraph 1 of the IASB Framework, and paragraphs 1 to 3 of the UKSP, and find the following three subjects: conceptual frameworks, accounting standards, and accounting standards setting, of which the relationship with each other is debatable.

With respect to Chinese accounting, its fundamental reform aimed at replacing the Soviet accounting model with international practices was started by the implementation of a conceptual framework, i.e. the 1992 Basic Standard. Furthermore, along with the issuance of a new complete series of 38 Specific Standards, the 1992 Basic Standard has been extensively revised and changed into the 2006 Basic Standard, which, for the first time, explicitly includes investors in the list of users of financial reports (Article 4 of the 2006 Basic Standard); introduces the asset and liability view about income (ibid, Article 30 and 31); whilst accounting elements are generally required to be measured at historical cost, accounting measurement bases also comprise replacement cost, net realisable value, present value and fair value (ibid, Article 42 and 43), in contrast with the 1992 Basic Standard that only allows historical cost (Article 19 of the 1992 Basic Standard). These amendments, together with many other significant changes in the 2006 Basic Standard, may indicate a trend towards making the Chinese conceptual framework converge with international ones, particularly the IASB Framework. This thesis cannot cover every facet of conceptual frameworks, but only could try to study what the role of the 2006 Basic Standard in Chinese GAAP is, for it may help predict whether the IASB Framework, along with IASB GAAP, will be directly applied in China in the future. In order to find the answer, the main content and function of Chinese and international conceptual frameworks will be compared in this chapter. A note about this chapter is that although the heading of this chapter is 'a discussion of conceptual frameworks', the measurement part of conceptual frameworks will not be discussed in this chapter.

1. global experience

The IASB Framework, which was issued by the IASC and adopted by the IASB, belongs to a family of conceptual frameworks that derives from the US ones. (Conceptual frameworks originated in the US.) The major early studies mentioned in SFAC 1 (paragraphs 57 and 60 of SFAC 1) include Accounting Principles Board (APB) Statement 4 and the Trueblood Report (American Institute of Certified Public Accountants (AICPA), 1973). Relying substantially on the Accounting Research Study No. 7 *An Inventory of Generally Accepted Accounting Principles* (written by Grady and published by the AICPA in 1965), in 1970 the APB released its Statement No. 4 *Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises* (APB Statement 4), which basically describes existing practice at that time and does not lay a foundation for setting standards. To respond to criticism for being without guidance on tackling old and new unresolved questions, in contrast to the inductive approach adopted in APB Statement 4, the Study Group on the Objectives of Financial Statements, which was set up by the AICPA and named the Trueblood committee after its chairman, Robert Trueblood, took a deductive, normative approach to prescribing the way things ought to be in its report *Objectives of Financial Statements*, commonly known as the Trueblood Report. Both APB

Statement 4 and the Trueblood Report pertain to objectives, as the former starts with identifying objectives of accounting, and the latter lists 12 objectives of financial statements. Most and Winters (1977) find that the above two sets of objectives are broadly similar. The FASB's conceptual framework project also began by considering objectives through the release of SFAC 1 *Objectives of Financial Reporting by Business Enterprises* in 1978, the foundation of which is the Trueblood Report (Appendix A of SFAC 1). The following several paragraphs will evaluate principal aspects of the FASB's conceptual frameworks.

SFAC 1 establishes the objectives of general purpose external financial reporting by business enterprises (paragraph 1 of SFAC 1). Financial reporting includes financial statements and other means of communication that provide accounting information (ibid, paragraph 7). From the explanation in paragraph 32 of SFAC 1 it may be inferred that the objectives outlined in SFAC 1 are not parallel and there is a logical sequence among them. The primary objective is stated as follows: 'Financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit, and similar decisions' (ibid, paragraph 34). In order to achieve this general overriding objective, a more specific objective is set: '[F]inancial reporting should provide information to help investors, creditors, and others assess the amounts, timing, and uncertainty of prospective net cash inflows to the related enterprise' (ibid, paragraph 37). To gain information on cash flows, the third objective is specified: 'Financial reporting should provide information about the economic resources of an enterprise, the claims to those resources, and the effects of transactions, events, and the circumstances that change resources and claims to those resources' (ibid, paragraph 40). In this connection, the following details are set out: Financial reporting should provide information about an enterprise's economic resources, obligations, and owners' equity, which provides users with indicators for future cash flows and the firm's financial strengths and weaknesses (ibid, paragraph 41). Financial reporting should provide information about an enterprise's financial performance during a period; the primary focus of financial reporting is information about an enterprise's performance provided by measures of earnings and its components (ibid, paragraphs 42 and 43). Earnings based on accrual accounting generally provide a better indication of enterprise performance and future cash flows than current cash receipts and payments, because, in determining earnings, accrual accounting recognizes transactions and events as they occur without regard to cash receipts and outlays (ibid, paragraph 44). Financial reporting should give assessment of management's stewardship (ibid, paragraph 50); since earnings, which are commonly used for assessing management's stewardship, are affected by factors other than current management performance, earnings may not be a reliable indicator of management performance (ibid, paragraphs 51 and 53).

Apart from the decision usefulness function of financial reporting, another long-established objective of accounting or financial statements is the stewardship of management, which is explained by Hawkins (1971: 58 in Chambers, 1995: 68) as follows: 'Owners entrust funds to management and management is expected to use these funds wisely. Periodically, management must report to the owners the results of management's actions. Financial statements are one of the principal means whereby management fulfils this reporting responsibility'. Ijiri (1967) and many other accounting scholars (see Chambers, 1995: 67 and 68) argue for the requirements of stewardship to be the primary and paramount purpose of accounting; and accordingly, stand up for the historical cost accounting model, which is based on actions actually taken by a firm, and thus facilitates the report on the stewardship. (The validity of this viewpoint will be assessed in the next chapter.) As cited above, SFAC 1 focuses on being useful for making economic decisions, and lays much less emphasis on assessing the stewardship of management. Dopuch and Sunder (1980) explain that the objectives of a social activity, including accounting, can be variously interpreted as functional objectives, common objectives, and dominant group objectives; among which the third interpretation means that the objectives of a social activity is the objectives of an individual or subset of all individuals in the society who are able, through whatever mechanism, to impose their will on all others involved in the activity. Obviously, this interpretation cannot be used if the dominant group does not have the power to impose its will on the society. In relation to SFAC 1, the FASB accept a user-primacy notion, i.e. the dominant group approach, in the selection of objectives which ignores firm managers' and auditors' interests. Since there is little evidence that the user group has the power to impose its preferences on financial accounting and, moreover, objectives preferred by various parties such as users, management and auditors are heterogeneous, the objectives in SFAC 1 are unworkable and will be ignored in future rule-making activities. In addition, Solomons (1986) points out that SFAC 1 takes an extra narrow view owing to the fact that it excludes altogether the interests of other groups with an interest in enterprise productivity, such as labour and the tax authority; and it also ignores the 'reporting enterprise activities affecting society' objective, which is recognized in the Trueblood Report.

SFAC 2 identifies the characteristics that make accounting information useful for decision making. Those characteristics or qualities can be viewed as a hierarchy, with usefulness for decision making of most importance (paragraph 32 of SFAC 2). However, paragraph 34 of SFAC 2 gives an explanation of an important limitation of the hierarchy, whereby 'while it does distinguish between primary and other qualities, it does not assign priorities among qualities. The hierarchy should be seen as no more than an explanatory device, the purpose of which is to clarify certain relationships rather than to assign relative weights'. Nevertheless, relevance and reliability are the two primary qualities that make accounting information useful (ibid, paragraph 33). Financial information must be both relevant and reliable to be useful; though, ideally, the choice of an accounting alternative should produce information that is both more reliable and more relevant, it may be necessary to sacrifice some of one quality for a gain in another. The trade-offs are made in view of the relative importance of the characteristics; and this relative importance is for specific users with particular needs to decide (ibid, paragraphs 42, 45 and 90). Relevance is defined in the glossary of terms as 'the capacity of information to make a difference in a decision by helping users to form predictions about the outcomes of past, present, and future events or to confirm or correct prior expectations'. To be relevant, information must be timely and it must have predictive value or feedback value or both. In other words, relevant information must be able to help the user make better forecasts of the future or better evaluations of the past. Reliability is described in the glossary as 'the quality of information that assures that information is reasonably free from error and bias and faithfully represents what it purports to represent'. To be reliable, information must have representational faithfulness and it must be verifiable and neutral (ibid, page 10 and paragraph 33). Comparability, which includes consistency, is a secondary quality that interacts with relevance and reliability to contribute to the usefulness of information (ibid, page 5). Paragraph 116 of SFAC 2 makes the point that comparability should not be pursued at the expense of relevance or reliability. Paragraphs 117 and 121 of SFAC 2 give a description that consistency 'is a necessary but not a sufficient condition of comparability', in other words, consistency does not assure comparability; and true comparability is the result of 'the representational faithfulness of the measurements used, rather than simply the unchanging nature of the measurement rules or the classification rules'. Two constraints are included in the hierarchy: materiality is a 'threshold for recognition', and benefits exceeding costs is a 'pervasive constraint' for all qualities (ibid, Figure 1 on page 20). Paragraphs 123, 126 and 129 of SFAC 2 illustrate that materiality depends on the relative size of an item and its nature, and requires judgment. Paragraph 136 of SFAC 2 acknowledges that it is extremely difficult to measure the costs and benefits of information; paragraph 140 of SFAC 2 continues recognizing that it is also difficult to ensure that 'the burden of costs and the incidence of benefits' are distributed fairly. A traditional accounting doctrine is conservatism or prudence, which is a reaction to uncertainties and risks that are inherent in business and economic activities typically by way of a deliberate and consistent understatement of net assets and profit. However, such understatements often bring on overstatements of earnings subsequently, and therefore introduce a bias in financial reporting and conflict with qualitative characteristics, such as representational faithfulness, neutrality and comparability (ibid, paragraphs 92-95). For the above reasons, as stated in SFAC 2, conservatism is not a quality that makes accounting information useful.

Representational faithfulness, an ingredient of the primary quality reliability, is defined in SFAC 2 as 'correspondence or agreement between a measure or description and the phenomenon it purports to represent' (paragraph 63 of SFAC 2). Bell (1993, in 1997: 75-86; 1997: xv-xx) proposes that the notion of representational faithfulness can be given independent status as a fundamental concept on the following grounds. In SFAC 2, reliability has two distinct and quite different connotations: verifiability, having to do essentially with trustworthy measurability; and representational faithfulness, having to do with the intrinsic nature of what is to be measured as reliably as possible. Relevance only conflicts with the measurement verifiability aspect of reliability, for example, historical costs have little relevance but have a high degree of measurable reliability, i.e. ease and accuracy of verification; but representational faithfulness and relevance are complementary, considering that the latter is heavily dependent upon the former, hence both help to make accounting information useful for decision making. Moreover, neutrality can be located directly under verifiability, rather than under reliability in general, for the reason that neutrality can be diversely construed as being neutral in the matter of 'economic consequences' or neutral in terms of 'financial reporting'; however, having identical economic consequences for all concerned is impossible. On top of that, neutrality relates to absence of bias in the verification process (Bell, 1997: xvii and xviii, citing Solomons, 1989, in 1997). On the subject of using the qualitative characteristics in accounting policy choices, Joyce et al.'s (1982) survey of 26 former policy makers, among whom 20 were once members of the APB, 3 had worked for the FASB, and 3 had served on both boards, reveals that there is considerable disagreement on not only the denotations but also the importance rankings of the characteristics listed in SFAC 2. In spite of the fact that the Statement gives different people much leeway to make divergent interpretations, Miller et al. (1994: 107) conclude that SFAC 2 provides a set of definitions that the Board and its constituents can and do use to communicate with each other, and can be considered worthwhile for that reason alone. Nowadays the ideas of choice, meaning and significance of qualities are still being developed, and no clear consensus has been reached.

The IASB Framework and the US conceptual frameworks are broadly similar in regard to the topics of objectives and qualitative characteristics. Some special features of the IASB Framework are given below. The IASB Framework states that '[t]he objective of financial statements is to provide information about the financial position, performance and changes in financial position of an entity that is useful to a wide range of users in making economic decisions' (paragraph 12 of the IASB Framework). Regarding 'a wide range of users', the IASB Framework identifies seven categories of users and their information needs, which encompass investors, employees, lenders, suppliers, customers, government agencies and the public (ibid, paragraph 9). But despite that, the IASB Framework argues that '[w]hile all of the information needs of these users cannot be met by financial statements, there are needs which are common to all users. As investors are providers of risk capital to the entity, the provision of financial statements that meet their needs will also meet most of the needs of other users that financial statements can satisfy' (ibid, paragraph 10), without providing any explanation for this claim. In order to meet their objectives, financial statements are prepared on the accrual basis of accounting and normally on the going concern basis (ibid, paragraphs 22 and 23). As for qualitative characteristics of financial statements, the four principal ones are understandability, relevance, reliability and comparability (ibid, paragraph 24). In contrast with SFAC 2, prudence is mentioned as a component of reliability, along with faithful representation, substance over form, neutrality and completeness. Paragraph 37 of the IASB Framework requires that '[p]rudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated'. However, the notion of prudence in the IASB Framework is subject to neutrality, and is in a softened form since deliberate understatement of assets or income or overstatement of liabilities or expenses is explicitly disallowed (ibid, paragraph 37).

The FASB and the IASB have undertaken a joint project since 2005 to develop a common and improved conceptual framework as part of the process of convergence of the two sets of standards. In July 2006, the FASB, together with the IASB, published a discussion paper *Preliminary Views on an improved Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics of Decision-Useful Financial Reporting Information*, which was followed by an exposure draft *Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics and Constraints of Decision-Useful Financial Reporting Information* (the 2008 Conceptual Framework Exposure Draft) published in May 2008. Some main points of that 2008 exposure draft are reproduced below.

> OB2. The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to present and potential equity investors, lenders, and other creditors in making decisions in their capacity as capital providers. Information that is decision useful to capital providers may also be useful to other users of financial reporting who are not capital providers.
>
> QC2. Economic phenomena are economic resources, claims to those resources, and the transactions and other events and circumstances that change them. Financial reporting information depicts economic phenomena (that exist or have already occurred) in words and numbers in

financial reports. For financial information to be useful, it must possess two fundamental qualitative characteristics – relevance and faithful representation.

QC3. Information is relevant if it is capable of making a difference in the decisions made by users in their capacity as capital providers. Information about an economic phenomenon is capable of making a difference when it has predictive value, confirmatory value, or both….

QC7. To be useful in financial reporting, information must be a faithful representation of the economic phenomena that it purports to represent. Faithful representation is attained when the depiction of an economic phenomenon is complete, neutral, and free from material error….

QC13. Once relevance is applied to determine which economic phenomena are pertinent to the decisions to be made, faithful representation is applied to determine which depictions of those phenomena best correspond to the relevant phenomena….

QC14. As fundamental qualitative characteristics, relevance and faithful representation work together to contribute to the decision usefulness of information in different ways. A depiction that is a faithful representation of an irrelevant phenomenon is not decision useful, just as a depiction that is an unfaithful representation of a relevant phenomenon results in information that is not decision useful….

QC15. Enhancing qualitative characteristics are complementary to the fundamental qualitative characteristics. Enhancing qualitative characteristics distinguish more-useful information from less-useful information. The enhancing qualitative characteristics are comparability, verifiability, timeliness, and understandability….

BC2.19. …To represent legal form that differs from the economic substance of the underlying economic phenomenon could not result in a faithful representation. Accordingly, the proposed framework does not identify substance over form as a component of faithful representation because to do so would be redundant.

BC2.21. …Introducing biased understatement of assets (or overstatement of liabilities) in one period frequently leads to overstating financial performance in later periods – a result that cannot be described as prudent. This is inconsistent with neutrality, which encompasses freedom from bias. Accordingly, the proposed framework does not include prudence or conservatism as desirable qualities of financial reporting information.

(extracted from the 2008 Conceptual Framework Exposure Draft, italics omitted)

One could argue that the 2008 Conceptual Framework Exposure Draft excludes the management's stewardship from an objective of financial reporting, and ignores a trade-off between different levels of relevance and faithful representation (see American Accounting Association (AAA)'s Financial Accounting Standards Committee (FASC) (2007) and Whittington (2008) for discussions about the earlier 2006 discussion paper). The next section examines definitions of assets in international and Chinese conceptual frameworks.

2. assets

(1) definitions in international conceptual frameworks

SFAC 6 *Elements of Financial Statements*, which was issued in 1985 and replaced SFAC 3 *Elements of Financial Statements of Business Enterprises*, identifies and defines the various component parts of financial reporting that are used for measuring performance and status of an entity, namely assets, liabilities, equity, investments by owners, distribution to owners, comprehensive income, revenues, expenses, gains, and losses. There are ten interrelated elements altogether (pages 6 and 7 of SFAC 6). Paragraphs 20 and 21 of SFAC 6 are specific about the articulation of the elements. One type of elements which consists of assets, liabilities and equity describes amounts of economic resources held or owed by an entity at a specific moment; the other type which comprises all other elements describes increases and decreases in economic resources over a period. The interrelationship between the two types of elements (see the diagram on page 25 of SFAC 6) denotes articulation; further, financial statements articulate with each other, so that statements that show elements of one type depend on statements that show elements of the other type and vice versa. SFAC 6 gives prominence to assets as the most fundamental element of financial statements, on the grounds that, firstly, assets or economic resources are the lifeblood of a business enterprise, and the primary reason behind the existence of an enterprise is to process, i.e. to acquire, use, produce, and distribute assets; and secondly, the definitions of all the other elements are derived from the ones of assets and liabilities. In addition, liabilities depend on assets because liabilities are obligations to pay or deliver assets (ibid, paragraphs 11 and 15; see also Storey and Storey, 1998: 72 and 123). Paragraphs 9 to 19 and 27 of SFAC 6 imply that economic resources and assets are interchangeable terminologies. This interpretation should also be consistent with other SFACs such as paragraph 40 of SFAC 1, cited above. Furthermore, SFAC 6 emphasises that the definitions are concerned with the essential characteristics of elements, and 'to be included in a particular set of financial statements, an item must not only qualify under the definition of an element but also must meet criteria for recognition and have a relevant attribute that is capable of reasonably reliable measurement or estimate' (ibid, paragraphs 22 and 23). Notably, between the recognition criteria in SFAC 5 and the definitions in SFAC 6, there may be inconsistencies, which may further result in the fact that the former sometimes overrides the latter (See Rosenfield, 2006: 221).

In view of the importance of the concept of assets, this section will specifically examine several definitions of assets in literature. In addition, some important features of different conceptual frameworks may also be observed from the assets segment. APB Statement 4 makes a preliminary but not very successful attempt to define assets as 'economic resources of an enterprise that are recognized and measured in conformity with generally accepted accounting principles. Assets also include certain deferred charges that are not resources, but they are recognized and measured in conformity with generally accepted accounting principles' (paragraph 132 of APB Statement 4). Storey and Storey (1998: 50 and 51) argue that the second sentence of that definition breaks the relationship between assets and economic resources, and makes an asset anything GAAP recognize and measure as assets, including what-you-may-call-its. A brief explanation of what-you-may-call-its is given below. Stemming from the conventional notion of 'proper matching of costs with revenues', the calculation of periodic net income becomes the focal point of accounting, thereby reporting some deferred charges/credits that may not have the nature of assets/liabilities in the balance sheet as assets/liabilities. Sprouse names those deferred charges or credits what-you-may-call-its, and concludes that income smoothing ('income equalization' in the original text) is the prime motive behind those practices (ibid: 54-66; Sprouse, 1966). The APB Statement 4's definition is criticized for actually defining nothing and being circular, since it is exactly the GAAP formulating body to determine what assets would be in GAAP (Storey and Storey, 1998: 50). Nonetheless APB Statement 4 merely describes what assets are, not what assets should be; SFAC 6 provides a prescriptive definition of assets as 'probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events' (paragraph 25 of SFAC 6). Immediately following the definition, paragraph 26 of SFAC 6 points up three essential characteristics of an asset, which consists of future economic benefits, controlled by a particular entity, and occurrence of a past transaction or event. Storey and Storey

(1998: 124) comment that '[t]he definition indicates the appropriate questions to ask in trying to decide whether or not a particular item is an asset: Is there a future economic benefit? If so, to which entity does it belong? What made it an asset of that entity?'. It is noteworthy that the FASB's definition places heavy emphasis on future economic benefit as the essence of an asset (paragraphs 27-31 and 172 of SFAC 6), and concomitantly affirms that, to be an asset, an item has to be the result of transactions or other events or circumstances that have already occurred (ibid, paragraphs 190 and 191). Macve (1981, reproduced in 1997: 77-79 and 118, note that 1981 is prior to the issue of SFAC 5) reasons that definitions of elements, not only the asset one, are unlikely to 'be helpful … in analyzing and resolving new financial accounting issues as they arise' (page 8 of SFAC 6), for the definition gives characteristics necessary for something to qualify as an asset, but these characteristics are not sufficient to decide whether it is an asset, this also requires consideration of 'recognition criteria'. Schuetze (2001) criticizes the FASB's definition of assets as being too abstract and vague to be used for solving problems. For example, although SFAC 6 states that costs themselves are not assets (paragraph 179 of SFAC 6), in practice it is a cost that is identified as an asset such as direct-response advertising cost, even though the probable future economic benefit of a successful direct-response advertising campaign bears little or no relationship to the cost incurred. (The relevant US GAAP is AICPA Statement of Position (SOP) 93-7 *Reporting on Advertising Costs*.) In addition to criticizing 'the cost per se is the asset syndrome', Schuetze posits that only real things should be counted as assets, not abstract future economic benefits; and suggests the following definition: 'cash, contractual claims to cash, things that can be exchanged for cash, and derivative contracts having a positive value to the holder thereof'. For all censure, the FASB's definition of assets would be the provenance of the other conceptual frameworks' definitions.

The IASB Framework identifies five elements of financial statements and divides them into two groups: assets, liabilities and equity are elements relating to financial position, and income and expenses are related to measurement of performance (paragraph 47 of the IASB Framework). An asset is defined as 'a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity' (ibid, paragraph 49(a)). Paragraph 50 of the IASB Framework states that the definition of an asset identifies its essential features but does not attempt to specify the criteria that need to be met before it is recognised in the balance sheet, thus the definition embraces items that are not recognised as assets in the balance sheet because they do not satisfy the criteria for recognition. The recognition criteria set out in paragraph 83 of the IASB Framework are that an item that meets the definition of an element should be recognised if: (a) it is probable that any future economic benefit associated with the item will flow to or from the entity; and (b) the item has a cost or value that can be measured with reliability. An apparently corresponding application of this definition is the key recognition criteria for an intangible asset, including identifiability, control, future economic benefits and reliable measurability of cost (paragraphs 11-23 of IAS 38 *Intangible Assets*). IAS 38 stipulates that internally generated brands shall not be recognised as intangible assets because expenditure on those brands cannot be distinguished from the cost of developing the business as a whole (ibid, paragraphs 63 and 64). Some scholars believe that the historical cost of developing a brand actually could be recognised, for instance, such activities as advertising, incurring extra expenditure on raw materials to create a 'better than average' product, giving refunds to dissatisfied customers where there was no legal duty to do so, and so on would have events or transactions associated with themselves. But it is generally impossible to link those events or transactions directly to the future economic benefits embodied in the brand as it exists at any given moment and therefore brands are not recognised as assets (see Rutherford, 2000: 90). Assets, liabilities, ownership interest, gains, losses, contributions from owners, and distributions to owners are elements identified in the UKSP (paragraph 4.2 of the UKSP). The UKSP defines assets as follows: 'Assets are rights or other access to future economic benefits controlled by an entity as a result of past transactions or events' (ibid, paragraph 4.6). The UKSP also explains that in the initial recognition process, there are two broad categories of uncertainty that could arise: a) element uncertainty, which involves uncertainty whether an item exists and meets the definitions of the elements of financial statements; and b) measurement uncertainty, which concerns the appropriate monetary amount at which to recognise the item (ibid, paragraph 5.12). Compared to the IASB Framework, the UKSP more understandably differentiates between uncertainty attaching to the existence of an asset and its measurement (see Whittington, 2008). While the above three definitions of assets are broadly similar, accounting treatment of specific issues may be dissimilar in their respective GAAP. For example, development activity fairly certainly can generate future economic benefits, but identifying the size and timing of benefits is difficult. SFAS 2 *Accounting for Research and Development Costs* (issued before the US conceptual framework) requires that development costs are all expensed; IAS 38 stipulates that costs incurred in the development phase should be capitalised if expenditure meets the recognition criteria; under the UK standard Statement of Standard Accounting Practice (SSAP) 13 *Accounting for Research and Development* (issued before the UKSP), development expenditure can be either capitalised or expensed immediately, if certain conditions are satisfied (note: SSAPs are issued by the Accounting Standards Committee (ASC), which is the predecessor of the ASB).

(2) definitions in Chinese conceptual frameworks

The assets element in Chinese conceptual frameworks will be examined next. The 1992 Basic Standard introduces the concept of assets to Chinese accounting. Extracts from the assets chapter are as follows: 'Article 22. Assets are economic resources, which are measurable by money value, and which are owned or controlled by an enterprise, including all property, rights as a creditor to others, and other rights. Article 30. …Fixed assets shall be accounted for at historical cost as obtained. Interest on loans and other related expenses for acquiring fixed assets, and the exchange difference from conversion of foreign currency loan, if incurred before the assets not having been put into operation or after been put into operation but before the final account for completed project is made, shall be accounted as fixed assets value…'. In that chapter of the 1992 Basic Standard, the definition of assets takes just 3 lines, while the other over 100 lines are all detailed rules which are similar to the one shown above. Moreover, the 1992 Basic Standard does not further expound on the attributes of the definition, does not attend to recognition criteria, and does not recognise that assets result from past events and are expected to result in future economic benefits, which are included in international conceptual frameworks (Davidson, 1996). Both in content and in form, the assets part of the 1992 Basic Standard is incomplete, especially in comparison with international conceptual frameworks; or to say in another way, it is a conceptual framework with unique Chinese characteristics.

Miller et al. (1994: 88-92) suggest that three different types of conceptual frameworks could be developed. The first one is a descriptive framework, which is developed by first examining what is being done in practice and then moving to higher level abstractions, i.e. by an inductive approach. A descriptive framework tends to keep existing practices intact, however, it cannot ensure that the practice being used is the best one that can ever be used and cannot reach a consensus on why it is happening. The second type is a prescriptive framework, which is developed by starting with a few general concepts and working down through their implications to statements of what ought to be done in practice, or in a more technical term, by a deductive method. A prescriptive framework is capable of uncovering areas in existing practice that can be improved and can be more easily applied to new situations, but such a framework is difficult to compile mainly because it sets out to achieve the resolution of all problems at the same time, moreover, its concepts may be perceived as to be too abstract to be applicable. The other type is a conceptual framework that defines commonly used terms. Those definitions will not eliminate debates, but will help the participants clarify the issues to be debated. It could be argued that the 1992 Basic Standard can be seen as descriptive, since it is largely drawn from existing accounting theory and practice abroad; meanwhile, it could be a prescriptive conceptual framework, as what it describes was largely new in China at that time; in addition, it outlines some basic terms such as the aforementioned definition of assets. As a result, it is difficult to find what type of conceptual framework the 1992 Basic Standard belongs exclusively to (Xiao and Pan, 1997). In spite of that, it is worthy of noticing that it is generally believed that a conceptual framework should provide a set of general and fundamental principles such as objectives, assumptions, and so forth, no matter what type it could be; on the other hand, accounting standards normally involve operational rules for specific matters. As the above quotation from the assets chapter have shown, the 1992 Basic Standard is a mixture of a conceptual framework and an accounting standard (Xiao and Pan, 1995: 187 and 188). This kind of arrangement may make the 1992 Basic Standard internally inconsistent. For instance, following the definition of assets in Article 22, Articles 23, 24 and 28 of the 1992 Basic standard stipulate that assets are normally divided into current assets, long-term investments, fixed assets, intangible assets, deferred assets and other assets; current assets include cash, cash deposits, short-term investments, accounts receivable, prepayments, and inventories, etc.; inventories refer to merchandise, finished goods, semifinished goods, goods in process, and all kinds of materials, fuels, containers, low-value and perishable articles and so on. For one thing, the 1992 Basic Standard cannot include all rules for every item listed; for another, some specific items within the assets category may not fit the definition of assets in the same chapter.

The 1992 Basic Standard defines revenue as follows: 'Revenue refers to the financial inflows to an enterprise as a result of the sale of goods and services, and other business activities of the enterprise, including basic operating revenue and other operating revenue' (Article 44 of the 1992 Basic Standard). In contrast, the IASB Framework defines income, which encompasses both revenue and gains, as 'increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants' (paragraph 70(a) and 74 of the IASB Framework). The US conceptual frameworks also interpret revenue as an increase in assets, a decrease in liabilities or some combination of the two (paragraph 78 of SFAC 6). Visibly, the 1992 Basic Standard takes the revenue and expense view, in contrast to the asset and liability view on which international conceptual frameworks are based. A basic explanation of these two polarising views is that, in choosing an accounting model, principally in defining the elements of accounting and in establishing recognition criteria, two views of income are available (note: income in this sense is called profit and loss in Chinese Basic Standards, but means the difference between income and expenses in the IASB Framework). The revenue and expense view holds that income is an indicator of performance of an enterprise and its management, accordingly, this view relies on proper matching and nondistortion of periodic income to allocate costs and revenues of actual transactions or events among different periods. Any cost incurred in a period that does not match that period's revenue is then carried forward in the balance sheet as an asset. In contrast, the asset and liability view sees income as an enhancement of wealth or command over economic resources. In this view, the impact of a transaction or event on the value of assets or liabilities is measured first; any item that does not affect assets or liabilities, in other words, does not meet the definition of assets and liabilities, is excluded from the balance sheet, and instead, directly put in the income statement. Income is then determined in terms of such as assets created and expenditure incurred. In a word, the revenue and expense view measures income directly by measuring revenues and expenses, and income is interpreted as 'the difference between revenues for the period and the expenses of earning those revenues'; in contrast, the asset and liability view measures income indirectly by measuring changes in the assets and liabilities, and income is interpreted as 'the difference between the excess of assets over liabilities at the end of a period and the excess at the beginning of the period' (see Solomons, 1989, in 1997: 22-25; 1997: 101-106; Storey and Storey, 1998: 76-85). Solomons (loc. cit.) strongly advocates the asset and liability view for the following reasons. The revenue and expense view opens the door to income smoothing by leaving management free to recognize and include deferred debits and credits that are not assets and liabilities to the balance sheet. In consequence, the revenue and expense view threatens the integrity of the balance sheet and its value as a useful statement of showing an entity's financial position, owing to the fact that not all of the items in the balance sheet are genuine assets and liabilities. In addition, even under the revenue and expense view, revenues and expenses have to be defined in terms of changes in assets and liabilities. To answer the comment that the asset and liability view tends to make profit a more volatile figure and does not well represent 'sustainable income', Solomons attacks that 'sustainable income' is not an accounting concept and volatility is a fact of life. Storey and Storey (1998: 78-80) review the conceptual primacy of assets and liabilities in the US conceptual frameworks. One reason for the rejection of the revenue and expense view is that revenues and expenses could not be independently defined if without assets and liabilities, otherwise, only by resorting to subjective guides such as proper matching; another reason is that the asset and liability view makes it clear that only the underlying economic resources and obligations of an enterprise can meet the definitions of assets and liabilities, and only items that increase or decrease the wealth of an enterprise can meet the definition of income and its components, including revenues, expenses, gains, and losses.

The US Securities and Exchange Commission (SEC) issued a report titled *Study Pursuant to Section 108(d) of the Sarbanes-Oxley Act of 2002 on the Adoption by the United States Financial Reporting System of a Principles-Based Accounting System* (the 'SEC Report') and submitted it to Congress in July 2003. That report judges that the revenue and expense view is inappropriate for use in setting principles-based (note: 'objectives-oriented' in the original text, these two expressions essentially have the same denotation) standards owing to the fact that standards developed under the revenue and expense view, for example, a variety of specific revenue recognition standards, are ad hoc and incoherent. Furthermore, the SEC Report states that 'from an economic perspective, income represents a flow of, or change in, wealth during a period…. The accounting equivalent to identifying 'wealth' is identifying the assets and liabilities related to the class of transactions. This identification of wealth acts as a conceptual anchor to determining revenues and expenses that result from the flow of wealth during the period'; and therefore comes to the conclusion that the asset and liability view 'most appropriately anchors the standard setting process by providing the strongest conceptual mapping to the underlying economic reality'. The IASB and the FASB set up a joint project on revenue recognition in 2002. The primary purpose of that project is to clarify the principles for recognizing revenue and to provide a single revenue recognition model for eliminating inconsistencies in the existing standards and addressing future revenue recognition issues. A discussion paper *Preliminary Views on Revenue Recognition in Contracts with Customers* (the 2008 Revenue Recognition Discussion Paper) was published by the IASB in December 2008. Closely based on the asset and liability view, paragraph 2.35 of that discussion paper puts forward the following revenue recognition principle: 'For a contract with a customer, revenue is recognized when a contract asset increases or a contract liability decreases (or some combination of the two)'. This principle means that when an entity becomes a party to a contract with a customer, it should start to recognize performance obligations inherent in that contract as a liability and the corresponding rights to receive a consideration as an asset. Consequently, two alternative approaches to the initial measurement of performance obligations were analyzed. One approach is to measure performance obligations at a current exit price, which is the amount that the entity would have to pay to an independent third party to take over those obligations; another one is the original transaction price approach, which would measure performance obligations as the consideration promised by the customer. The 2008 Revenue Recognition Discussion Paper rejects the former and favours the latter. One reason for making this choice is that if the exit price of the performance obligations at initial recognition is less than the customer consideration, a portion of the total revenue would be recognized before any of the goods and services are provided under the current exit price approach. The IASB disagrees with this pattern of revenue recognition. By contrast, no revenue is recognized at contract inception by the original transaction price approach. The other reason given is that estimation of how much someone else might pay for the remaining performance obligations after deducting costs incurred in obtaining the contract is complex and those estimates are difficult to be validated. In contrast, the original transaction price is observable, and thus the risk of errors in estimation is reduced (paragraphs 5.14-5.33 of the 2008 Revenue Recognition Discussion Paper). Benston et al. (2006; 2006: 30-34, 261-270) question the conceptual primacy of the asset and liability view and the revenue recognition model based on changes in assets and liabilities. The main reasoning behind their view is as follows: Because of the fact that not all assets and liabilities on the balance sheet can be valued or periodically revalued at the same measurement attribute, presumably at their fair values, the asset and liability approach to dependently measuring net income cannot be achieved as a consistent conceptual approach in practice. Moreover, some of those fair values are determined in managerial judgments, which allow possible opportunistic manipulation by managers. For one thing, numbers based on estimates cannot be used in a trustworthy accounting system, as they cannot be audited; for another, very detailed rules for calculating those numbers would have to be imposed, but the point of excessive details contradicts the qualities of principles-based standards. By contrast, the revenue and expense view has several advantages, for example, under the traditional method of the determination of net income that is based on the matching and prudence concepts, in most cases, revenue is recognized on the occurrence of actual market transactions, and the amount of revenue earned is determined by the value of the asset received in exchange for the goods and services. In other words, the traditional model of revenue recognition features proper timing and reliable measurement. Besides, the revenue and expense approach has survived and developed over many years on the basis of tested experience, it seems likely that the costs of abandoning the revenue and expense approach and adopting the asset and liability one would exceed the benefits, both to accountants and investors.

Accounting for long-term construction contracts could be an example to show several different revenue recognition models. In general, a construction contract requires more than one accounting period for the completion, and therefore the timing of the recognition of revenue and profit becomes the primary issue in accounting for construction contracts. One way of dealing with this problem is the completed contract method, which recognizes revenue only after the contract is completed. This method could be justified on the grounds of the prudence and the realization convention. Realization means the process of converting noncash resources and rights into money or, more precisely, the sale of an asset for cash or claims to cash (paragraph 143 of SFAC 6). However, on account of the fact that, under most circumstances, the contractor has the legally enforceable right to require the customer to make progress payments during the construction period, the accounting treatment of recording a substantial amount of profit in one period but none over other periods may not give a fair presentation of the business activity of the reporting entity. In addition, managers can arbitrarily delay or speed up the completion date of a project, thereby controlling the profit they declare in any period. Alternatively, revenue is recognized under the percentage of completion method, which requires allocation of contract revenue and the contract costs incurred in reaching the stage of completion if the percentage of the completion of the contract can be reliably determined. This method follows the matching principle, and arguably can provide useful information on the extent of contract activity and performance during a period. Nevertheless, this principle for recognizing revenue as the work progresses is inconsistent with the principle for the sale of goods, which is that revenue should be recognized only when an entity transfers control and the risks and rewards of ownership of the goods to the customer. Moreover, the contractor can make aggressive estimates of progress towards completion and overstate the amount of revenue recognized (Mulford and Comiskey, 2002: 183 and 184; Alexander and Archer, 2007: 11.01-11.14; paragraphs 1.15 and 1.16 of the 2008 Revenue Recognition Discussion Paper). Under the proposed original transaction price approach that conforms to the asset and liability view, the assets and liabilities inherent in a construction contract are recorded equal to the amount the customer would pay on initial recognition. As to subsequent measurement, managers' estimation is needed to determine the allocation of part of the original transaction price to the remaining performance obligations at each financial statement date. Consequently, this proposed method gives managers too much leeway to misreport revenue (Benston et al., 2006: 268-270; paragraphs 5.25-5.44 of the 2008 Revenue Recognition Discussion Paper). Visibly, all of the above three approaches use some accounting criteria discussed in conceptual frameworks as a basis, in addition, all of them require estimates, and may be manipulated by managements. There is no consensus on the most rational or useful approach that can provide the most relevant information. In practice, IAS 11 and ASBE 15, both under the title *Construction Contracts*, recognize only the percentage of completion method; whereas US GAAP, sc. ARB 45 *Long-Term Construction-Type Contracts* and AICPA SOP 81-1 *Accounting for*

Performance of Construction-Type and Certain Production-Type Contracts, permits both the percentage of completion method and the completed contract method, and the former method is preferable and the latter one is reserved for circumstances when dependable estimates of progress towards completion, contract revenue and contract costs cannot be made. It is noticeable that the 2008 Revenue Recognition Discussion Paper avoids an analysis of the use of fair value, and no quick action on moving towards the asset and liability approach is expected.

In regard to Chinese accounting, the whole assets and revenue chapters of the 2006 Basic Standard are reproduced below.

> Chapter 3 Assets
>
> Article 20 An asset is a resource that is owned or controlled by an enterprise as a result of past transactions or events and is expected to generate economic benefits to the enterprise.
>
> 'Past transactions or events' mentioned in preceding paragraph include acquisition, production, construction or other transactions or events. Transactions or events excepted to occur in the future do not give rise to assets.
>
> 'Owned or controlled by an enterprise' is the right to enjoy the ownership of a particular resource or, although the enterprise may not have the ownership of a particular resource, it can control the resource.
>
> 'Expected to generate economic benefits to the enterprise' is the potential to bring inflows of cash and cash equivalents, directly or indirectly, to the enterprise.
>
> Article 21 A resource that satisfies the definition of an asset set out in Article 20 in this standard shall be recognized as an asset when both of the following conditions are met:
>
> (a) it is probable that the economic benefits associated with that resource will flow to the enterprise; and
>
> (b) the cost or value of that resource can be measured reliably.
>
> Article 22 An item that satisfies the definition and recognition criteria of an asset shall be included in the balance sheet. An item that satisfies the definition of an asset but fails to meet the recognition criteria shall not be included in the balance sheet.
>
> Chapter 6 Revenue
>
> Article 30 Revenue is the gross inflow of economic benefits derived from the course of ordinary activities that result in increases in equity, other than those relating to contributions from owners.
>
> Article 31 Revenue is recognized only when it is probable that economic benefits will flow to the enterprise, which will result in an increase in assets or decrease in liabilities and the amount of the inflow of economic benefits can be measured reliably.
>
> Article 32 An item that satisfies the definition and recognition criteria of revenue shall be included in the income statement.
>
> (extracted from the 2006 Basic Standard)

Obviously, from the previous citations, in contrast to the 1992 Basic Standard, the 2006 Basic Standard is no longer a hybrid of rules on detailed matters and a conceptual framework that should address fundamental issues; only are the normative elements retained in the new Chinese conceptual framework, which is substantially in step with international ones, especially being evidenced by the adoption of the asset and liability view. A direct application of this new definition of an asset could be the accounting treatment for the impairment of assets in ASBE 8, which was mentioned in chapter one. Conceivably, the old definition in the 1992 Basic Standard could not provide a rationale for impairment, principally because an asset is described as impaired when the economic benefits, which are generated by that asset to the enterprise, cannot still be reasonably expected. Nevertheless, the 1992 Basic Standard does not contain the 'expected to generate economic benefits' feature in its definition of assets (Article 22 of the 1992 Basic Standard, cited on page 74); and states clearly that '[t]he values of all assets are to be recorded at historical costs at the time of acquisition. The amount recorded in books of account shall not be adjusted even though a fluctuation in their value may occur…' (ibid, Article 19). However, the new interpretation of assets may not satisfactorily explain the prohibition of reversing impairment losses in Chinese GAAP. This issue will be discussed in more detail in the next chapter. As regards the characteristics of an asset in Article 20 of the 2006 Basic Standard, some criticisms are as follows: The 'past transactions or events' clause might highlight the conventional 'transaction based' idea of financial reporting, although the definition of assets is of economic focus. However, transactions could be taken merely as special classes of events, and more importantly, this clause could produce a game of 'hunt the event' rather than representing a significant factor in discriminating between assets and non-assets. As far as the 'expected to generate economic benefits to the enterprise' clause is concerned, in spite of the sense of future implied in 'expected', it circumvents the debatable 'future economic benefits' embraced by the IASB Framework. To put it briefly, the source of contention is chiefly because future economic benefits could make assets constitute future economic resources (the foregoing contents are referred both to Rutherford, 2000: 62-76, which is on the conceptual framework of the UK and to Booth, 2003, which is concerning the expired Australian conceptual framework).

The IASB and FASB conceptual framework joint project proposes a new definition: 'An asset is a present economic resource to which the entity has a present right or other privileged access' (quoted in Whittington, 2008). As opposed to the current definition in the IASB Framework (cited on page 72), two phrases 'as a result of past events' and 'from which future benefits are expected to flow' are deleted. Whittington (op. cit.) contends that the deletion may weaken the stewardship purpose of financial reporting and alter the current recognition criteria (cited on page 72), because the notion of 'transaction based accounting' is not emphasized, the reliability criterion related to recognition uncertainty becomes unimportant, and thus uncertainty is transferred from recognition to measurement. The conclusion of this section on assets is that the convergence of the Chinese conceptual framework with the international one is in progress; the definitions of assets made by each country bear their own characteristics and are certainly debatable whatever their wording and expressions; definitions could be used to interpret standards, but how to interpret them tends to be arguable. The next section will refer to the development process of Chinese conceptual framework.

3. the Chinese conceptual framework

(1) the asset and liability view

This section is in an attempt to study the staple of the 2006 Basic Standard by exemplifying. The most important change in the 2006 Basic Standard is arguably the adoption of the asset and liability view. To continue the example of deferred tax in the first chapter, among several methods of deferred tax, the deferral method is based upon the matching principle, specifically, in practice any reversal of the timing difference relating to an asset is reversed at the same rate of tax as the one applied to the originating timing difference on that asset. This method ensures that the tax expense, consisting of current and deferred parts, can properly match with the pre-tax accounting income that brings it about, thereby avoiding distortions of the income statement. Nevertheless, the total deferred tax provision in the balance sheet may be composed of deferred credits calculated at different prior period tax rates being used to recognize those deferred taxes, that is to say, the amount deferred is not affected when the tax rate changes. A liability is defined in the 2006 Basic Standard as 'a present obligation arising from past transactions or events which are expected to give rise to an outflow of economic benefits from the enterprise. A present obligation is a duty committed by the enterprise under current circumstances. Obligations that will result from the occurrence of future transactions or events are not present obligations and shall not be recognized as liabilities' (Article 23 of the 2006 Basic Standard). Obviously, the amount of the deferred tax account calculated in accordance with the deferral method is typical of what-you-may-call-its, but does not conform with the definition of a liability, since a liability will be revised simultaneously with the change of income tax rate, instead of being an amount saved as part of history. In order to prevent material distortions of the balance sheet, and more importantly, to ensure all items in the balance sheet fit the definitions of elements of financial statements, the liability method becomes an alternative, which is balance sheet oriented and aimed at making the best estimate of the obligation for taxes payable in future periods as the income tax liability on the balance sheet by taking account of changes in the rate of tax charged. Between the two liability methods, the income statement liability method focuses on the differences between accounting profit and taxable profit that originate in one period and reverse in one or more subsequent periods, namely timing differences; whereas the balance sheet liability method, which is the method demanded in the current Chinese and IASB GAAP, stipulates that deferred taxation should be provided for temporary differences, i.e. the ones between the carrying amount of an asset or liability in the balance sheet and its tax base. The rationale underlying the balance sheet liability method to account for deferred tax on temporary differences is that '[i]t is inherent in the recognition of an asset or liability that the reporting entity expects to recover or settle the carrying amount of that asset or liability. If it is probable that recovery or settlement of that carrying amount will make future tax payments larger (smaller) than they would be if such recovery or settlement were to have no tax consequences, an entity should recognize a deferred tax liability (deferred tax asset)…' (quoted from Objective of IAS 12; it is worth taking notice that the Chinese standard ASBE 18 does not include any analogous contents). In consequence of the above theoretical grounds, deferred taxes should be provided for asset revaluations, even if there might be no intention to sell the asset (Article 5 of ASBE 18 and Article 1 of the implementation guidance on ASBE 18; note: specific standards and the implementation guidance on them are equally effective in Chinese GAAP). Nonetheless, as the definition of a liability cited above has demonstrated, a future commitment does not generate a liability, or to rephrase it, the future taxable income is not the past event required by the definition of a liability in the 2006 Basic Standard and therefore a deferred tax liability (or asset) might not arise from a revaluation. Some critics may further attest that the whole deferred tax would be abolished as no liability is currently incurred at a balance sheet date (see Rosenfield, 2006: 434-436). Apart from whether to comply with the definition of a liability or not, another disputable point is probably that ASBE 18 does not allow the discounting of deferred tax assets and liabilities (Article 19 of ASBE 18). Because enterprises may not dispose of the asset for many years, and in reality most of them are inclined to further defer the deferred liability by continuous asset replacement, in the circumstances discounting the deferred tax could be deemed as a method to reflect the time value of money. With respect to the reason for not allowing discounting, the Chinese standard does not state anything, IAS 12 makes the following explanation: discounting should not be required on the basis that reliable calculation is impracticable or highly complex; neither should it be permitted on the basis that comparability between entities is necessary (paragraph 54 of IAS 12). It could be believed that the prohibition of discounting in IAS 12 is on the grounds of reliability, comparability and benefit exceeding cost considerations; and yet the above justification could also been held to be essentially pragmatic. As far as Chinese GAAP is concerned, firstly, the Chinese deferred tax standard does not embrace any contents about how the prescribed accounting treatment interconnects with the 2006 Basic Standard; secondly, it is difficult to apply the terms in the Chinese conceptual framework to resolve the question of whether deferred tax is a liability, and to expound the specific accounting procedures.

What should command attention is the similar formation in both Chinese and international conceptual frameworks, which takes users and their information needs as the starting points. It was mentioned previously in this chapter that the IASB Framework stresses that investors are the primary users of accounting information. In the respect of Chinese conceptual frameworks, the 1992 Basic Standard stipulates that 'accounting information must be designed to meet the requirements of national macroeconomy (author note: ipsissima verba in the English version) control, the needs of all concerned external users to understand an enterprise's financial position and operating results, and the needs of management of enterprises to strengthen their financial management and administration' (Article 11 of the 1992 Basic Standard). This short paragraph classifies three groups of users, and at the same time implies the objectives of financial reports. But for all that, the 1992 Basic Standard can neither explicitly specify the generally called users other than the government and corporate managers nor recognize potential differences in the information needs of various user groups. From certain possible reason for that, it may be inferred that all relevant parties have equal rights to the financial information of a company, accordingly, one set of financial statements could meet their different requirements; or that there is a hierarchy of users, among others, government is the primary user. Anyway, the 1992 Basic Standard commits no further discussion to user information needs (Xiao and Pan, 1995: 189-191; 1997). The 2006 Basic Standard approaches this topic as follows: 'The objective of financial reports is to provide accounting information about the financial position, operating results and cash flows etc. of the enterprise to the users of the financial reports, in order to show results of the management's stewardship, and assist users of financial reports to make economic decisions. Users of financial reports include investors, creditors, government and its relevant departments as well as the public' (Article 4 of the 2006 Basic Standard). Compared with the former conceptual framework, what is comprised in the 2006 Basic Standard is nearer to internationally accepted norms, specifically being: first, the enterprise's management, who should be the preparer in lieu of the user of financial statements, and whose information needs may not be the same as those of external users, is no longer a category of users; second, investors and creditors become user groups, and their information needs of assessing the stewardship of management and taking economic decisions are correspondingly laid stress on. Besides, the objective of serving the government in the macroeconomic administration might be no longer primary and key (or at least, taken literally), anyway, the government is still an important user. In wording, such an alteration to definition of users in the 2006 Basic Standard brings it some similarity to the FASB's SFAC 1 (quoted on page 61), which refers to both investors and creditors, not just only to investors. In contents, the new Chinese conceptual framework bears close resemblance to the UK conceptual framework (Chapter 1 of the UKSP) through its inclusion of both the assessment of stewardship and the economic decision making objectives. The cause of the above changes in the 2006 Basic Standard is fundamentally considered as an outcome of development in China's market economy, especially, in its capital market. Continuing the discussion about deferred tax in the previous paragraph, the concept of the time value of money signifies that a sum of liability which can be postponed for many years is definitely less than a sum due immediately, the utilization of discounting could demonstrate this economic difference. Therefore, from the aspect of serving investors' information needs, discounting of deferred tax balances should be permitted, in that case, investors could form a better view of future envision of a company. Alternatively, also from the aspect of serving investors' information needs, discounting should not be permitted, for the reason that managers may make use of discounting to boost earnings, and further, investors themselves could make the necessary adjustments for discounting anyway. This issue, along with the wider topic of discounting long-term liabilities, is complex and debatable. Apart from merely touching upon users and their needs in above cited Article 4, the 2006 Basic Standard like the 1992 Basic Standard does not continue with the discussion about this issue any more, so it is hard to measure whatever the influence exercised by the revisions of users on specific standards is. Further elaboration on income taxes is referred to Rosenfield (2006: 422-442), and Alexander and Archer (2007: 20.01-20.23).

On top of forbidding the deferral method in accounting for income taxes, another influence from the application of the asset and liability view may be disallowing the use of LIFO as a cost formula for inventories, which is mentioned in the first chapter. The LIFO method assumes that the last goods purchased are the first goods used or sold, thereby allowing the matching of current costs with current revenue and then possibly being better for periodic income calculation. But on the other hand, in a spell of changing prices, the use of LIFO is prone to misrepresent the inventories balance in the balance sheet, for closing inventories are usually measured at costs from earlier periods. In contrast, the first-in, first-out (FIFO) method reasonably is more advantageous to balance sheet purposes considering it is inclined to show ending inventories at their current costs. For the prohibition of LIFO, no explanation is provided in the Chinese standard ASBE 1; while the reason set out in IAS 2 is due to a lack of representational faithfulness of inventory flows in LIFO (paragraph BC19 of Basis for Conclusions, IAS 2), instead of preventing the damage to the balance sheet caused by the use of LIFO, however, physical flow is not an accounting concept and may not necessarily stand for the cost flow in the revenue generation process. There is one point which should be noticed that in a historical cost based accounting system for inventories, none of cost formula is commonly perceived as superior to other formulas in reflecting the true value of inventories. The above two examples of income taxes and inventories could display the effect on Chinese accounting standards exerted by the adoption of the asset and liability view and other changes in the 2006 Basic Standard.

In terms of the other facets of the Chinese conceptual framework, Chapter 1 of the 2006 Basic Standard specifies general provisions, which primarily comprise accounting entity, going concern, accounting period, monetary measurement, and accrual basis (from Article 5 to 9 of the 2006 Basic Standard in their given order); those internationally recognized accounting assumptions are successively mentioned in Article 4, 5, 6, 7 and 16 of the 1992 Basic Standard as well. On account of the introduction of the asset and liability view, the matching principle, which is described in the 1992 Basic Standard as that 'revenue shall be matched with related costs and expenses in accounting' (Article 17 of the 1992 Basic Standard), does not exist in the 2006 Basic Standard any longer. In comparison, the IASB Framework makes mention of the matching of costs with revenues, further, it points it up that the application of the matching concept does not allow the recognition of items in the balance sheet which do not meet the definition of assets or liabilities (paragraph 95 of the IASB Framework). In spite of the deletion of matching from the current Chinese conceptual framework, some particular accounting treatments in Chinese GAAP are still based on the matching principle. Citing such an example as above-mentioned, in accounting for construction contracts, ASBE 15 requires the percentage of completion method, which is derived from the principle of matching. Besides, it is mentioned in the first chapter that ASBE 16 requires that grants related to assets, which are government grants whose primary condition is that an entity qualifying for them should purchase, construct, or otherwise acquire long-term assets, should be presented in the balance sheet as deferred income, that is, a liability item, and treated as income over the life of the asset. This deferred income approach precisely abides by the matching convention, specifically speaking, government grants should be recognized as income over the periods necessary to match them with the related costs which they are intended to compensate. What merits attention is that, in the Chinese standard ASBE 16, there are no contents to delineate what conventions the accounting for government grants is founded on; the above explanation is extracted from paragraph 12 of IAS 20, which also allows the deferred income approach. Moreover, owing to the application of the matching principle, the deferred income method brings on an item shown as a liability that does not meet the definition of a liability in default of any present obligation that gives rise to outflow of resources. Meanwhile, one issue which deserves to be pointed out is that IAS 20 also permits the presentation of government grants related to assets as the deduction of the grant from the carrying amount of the asset, and the grant is recognized as income over the life of the depreciable asset by reducing the depreciation charge. This alternative is derived from matching as well, but it brings about no clear measurement basis for the asset because assets may be obtained under varying government policy; as a result, the matching convention may not be suitable for selecting different ways of treating a government grant (see Nobes, 2005). The two examples of construction contracts and government grants in this paragraph manifest that, in Chinese accounting, some of accounting standards might not be in accord with certain new regulations in the conceptual framework, in other words, the 2006 Basic Standard cannot elucidate specific standards very clearly.

(2) qualitative requirements

Chapter 2 of the 2006 Basic Standard puts forward qualitative requirements of accounting information, which mainly embrace faithful representation, relevance, understandability, comparability including consistency, substance over form, materiality, prudence, and timeliness (from Article 12 to 19 of the 2006 Basic Standard in sequence); these characteristics are close to the ones in conceptual frameworks of other jurisdictions. Similarly, qualitative characteristics acknowledged in the 1992 Basic Standard largely involve objectivity, uniformity including comparability, consistency, timeliness, understandability, prudence, and materiality (respectively indicated in Article 10, 12, 13, 14, 15, 18 and 21 of the 1992 Basic Standard; note: it may be claimed that, in the 1992 Basic Standard, accrual basis and matching are two general principles, which could be deduced connoting qualitative characteristics from the context, rather than accounting assumptions or terms; and, as above cited, Article 11 implies relevance). Xiao and Pan (1995: 191 and 192) make their criticism over the pertinent subjects in the 1992 Basic Standard, mainly as follows: one noticeable weakness of the qualitative characteristics described in the 1992 Basic Standard is that they are listed sequentially, but without any layering that could represent their relative importance, as manifested in other frameworks. Presumably, someone may believe that important weightings depend on their position in the sequential list; however, the 1992 Basic Standard fails to demonstrate its reasoning for such attachment of weightings, for instance, to spell out why objectivity is the most important attribute. Another important defect in the 1992 Basic Standard is that the conflicts between the characteristics are not acknowledged, as a consequence guidance on trade-offs among them is not provided. Furthermore, the 1992 Basic Standard does not offer any detailed and operational definition of the characteristics, for example, to describe what makes information comparable. Naturally, it cannot be expected that a trivial list of incomplete phrasing about characteristics is of great value to ensuring the quality of accounting information. The above disapproval of the features in the old conceptual framework is applicable to the present conceptual framework as well because of the 2006 Basic Standard's failure to elaborate any reference to how to use the qualitative characteristics in preparing and using financial reports except for a sequential list.

Meanwhile one point should be paid attention to is that, as observed from the experience of international conceptual frameworks, even if the 2006 Basic Standard contains reference, certain debate is almost unavoidable. For example, in the 2008 Conceptual Framework Exposure Draft (some paragraphs about qualitative characteristics are reproduced on pages 67 and 68), despite the fact that reliability is subsumed under faithful representation, hence averting the need for trade-off between relevance and reliability, the possibility of a trade-off between different levels of relevance and faithful representation may not be avertable all the same, just like the example of whether greater representational faithfulness could compensate for less relevance or not. (The answer appears to be not based on paragraph QC14.) The other questionable issues raised in the 2008 Conceptual Framework Exposure Draft include whether conservatism conflicts with neutrality or not, whether comparability is of the same importance as relevance and faithful representation or not, and so on (see Whittington, 2008; Peasnell et al., 2009). Those arguments about qualitative characteristics are really some platitudes of an aged scholar; notwithstanding, the Chinese conceptual framework merely touches on some characteristics and never broaches anything about the connection and contradiction between them.

In comparison to the 1992 Basic Standard, the 2006 Basic Standard contains the concept of substance over form in Article 16: 'An enterprise shall recognize, measure and report transactions or events based on their substance, and not merely based on their legal form' (note: in Chinese accounting regulations, substance over form emerges in Article 11 (2) of the 2000 System for the first time). Lease accounting could be regarded as an employment of the principle of substance over form. ASBE 21 *Leases* interprets terminologies as below-mentioned: 'A lease is an agreement whereby the lessor conveys to the lessee in return for rent the right to use an asset for an agreed period of time' (Article 2 of ASBE 21). 'A finance lease is a lease that transfers in substance all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred' (ibid, Article 5).

‘An operating lease is a lease other than a finance lease’ (ibid, Article 10). With reference to accounting treatment for finance leases, the original of Article 11 of ASBE 21 is that ‘at the inception of the lease, lessees should record the leased asset at an amount equal to the lower of the fair value of the leased asset and the present value of the minimum lease payments, record the gross amount of the minimum lease payments as the long-term account payable. The difference between the recorded amount of the leased asset and the liability should be recorded as unrecognized finance charges’ (note: translated by this writer; what deserves consideration is that this article is written in the form of doing double entry bookkeeping). To put it in another way, Chinese GAAP requires that lessees should recognize finance leases as assets and liabilities in their balance sheets; this stipulation of capitalizing finance leases should be on the foundation of the principle of substance over form, however, like all of the cases already exemplified in this section, the Chinese standard ASBE 21 does not speak of any word about how accounting for leases interconnects with the conceptual framework. There is one explanation, which concerns the utilization of the principle of substance over form in the accounting for lease transactions and is represented in paragraphs from 21 to 24 of IAS 17 *Leases*, which also prescribes capitalization of finance leases, as below: ‘Although the legal form of a lease agreement is that the lessee may acquire no legal title to the leased asset, in the case of finance leases the substance and financial reality are that the lessee acquires the economic benefits of the use of the leased asset for the major part of its economic life in return for entering into an obligation to pay for that right an amount approximating, at the inception of the lease, the fair value of the asset and the related finance charge’ (paragraph 21 of IAS 17). ‘If such lease transactions are not reflected in the lessee’s balance sheet, the economic resources and the level of obligations of an entity are understated, thereby distorting financial ratios. Therefore, it is appropriate for a finance lease to be recognized in the lessee’s balance sheet both as an asset and as an obligation to pay future lease payments’ (ibid, paragraph 22). In addition, in Chinese GAAP, the former *Leases* standard, which came into effect from 2001 and was applied to all business enterprises, requires that 'if a sale and leaseback transaction results in an operating lease, any difference between the sales proceeds and the carrying amount should be deferred and amortized according to the proportion of the lease payments during the lease term' (Article 37 of the 2001 Leases standard). To deal with the same sale and leaseback transaction that results in a situation of operating lease, ASBE 21 allows that gains and losses are recognized in profit in the current period if there is (conclusive) evidence that the transaction is established at fair value, otherwise the difference should be deferred and amortized similarly to the stipulation in the 2001 Leases standard (Article 32 of ASBE 21). The alteration in ASBE 21 agrees with the requirements in IAS 17 (paragraph 61 of IAS 17) and could be thought of as an application of the substance over form principle, because even though the sale and leaseback transaction is contracted as a package, if the leaseback is an operating lease, and the lease payments and the sale price are at fair value, there has in effect been a normal sale transaction and any profit or loss shall be recognized immediately (from paragraph 62 of IAS 17), ASBE 21 does not detail similarly. Incidentally, in comparison with the 2001 Leases standard, one of the conspicuous modifications in ASBE 21 is the use of fair values; the topic of fair value will be discussed in the next chapter.

The discussion on accounting for leases in this section refers to Nobes (2005) and Rosenfield (2006: 489-498). According to ASBE 21, a finance lease should be capitalized as an asset and a liability (Article 11 of ASBE 21, cited in last paragraph); while 'lease payments under an operating lease should be recognized as an expense in the income statement…' (Article 22 of ASBE 21), namely, nothing appears in the balance sheet. A company may have a motivation to classify a lease as an operating lease, thereby being able to use an economic resource that is off the balance sheet and the associated liability is omitted as well. In order to properly classify a lease, that is, to make the principle of substance over form feasible and to prevent the distortion of financial ratios, Chinese GAAP lays down the below requirements: apart from the above-mentioned Article 5 of ASBE 21, which provides a definition of a finance lease based on substance over form, the coming Article 6 establishes five criteria that individually or jointly will give rise to a lease being classified as a finance lease: for instance, the lease term is for the major part of the useful life of the leased asset even if title is not transferred; at the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased assets (Articles 6 (3) and (4) of ASBE 21). These non-numerical prescriptive criteria for classifying a finance lease signifies the principle of substance over form and are roughly similar to the examples of situations contained in paragraph 10 of IAS 17, whereas IAS 17 places an emphasis on the definition rather than examples that 'would normally' or 'could' lead to a finance lease (paragraphs 8, 10 and 11 of IAS 17). On the other hand, much as they all stem from the principle of substance over form, the definition denoted in Article 5 of ASBE 21 is considered vague, and the criteria detailed in Article 6 of ASBE 21 are deemed vague also, because of a lack of elucidation of the phrases such as 'major part of the useful life' and 'substantially all'. Possibly for the sake of resolving this problem, simultaneously, the implementation guidance on ASBE 21, which is one of the components of Chinese GAAP and equally effective to ASBE 21, defines 'major part' as usually equivalent to 75% or more of the useful life, and 'substantially all' as usually 90% or more of the fair value (Article 2 of the implementation guidance on ASBE 21). IAS 17 excludes numerical rules, whereas the US standard SFAS 13 *Accounting for Leases* takes comparable and numerical specifications as criteria for classifying leases (paragraph 7 of SFAS 13). But those technical bright lines in the implementation guidance on ASBE 21 may be arbitrary, as managers may manipulate leases into the operating category by designing contracts to avoid those numerical cut-off points. Furthermore, it is not clear which one, either the 'major part' or the 'usually 75% or more', should be the determining factor in the criteria for classifying a lease, as a consequence, lease accounting in Chinese GAAP is both vague and arbitrary.

This complication is probably contributed to the factor that ASBE 21 is founded on the principle of substance over form, which is inappropriate. Parenthetically, it is the exact legal form of the lease contract that gives rise to the lessee's obligation and to control over the leased asset, in other words, the legal form and the economic substance are not in conflict (Nobes, 2005). The more appropriate principles should be the definitions of an asset and a liability (respectively cited on page 82 and pages 84 and 85). Specifically, on entering a lease contract, the lessee gets control over a resource for a period, thus holds an asset that accords with the definition of an asset explicated in Article 20 of the 2006 Basic Standard; and the lessee assumes an obligation to make the rental payments alike, hence a liability that agrees with the definition of a liability characterized in Article 23 of the 2006 Basic Standard. In consequence, based on the definitions of an asset and a liability, the requirement to classify a lease as an operating lease or a finance lease would be abolished, and all leases would be capitalized. A substitute view for applying the asset and liability definitions is that the accounting model for leases should be consonant with the one for executory contracts, which is defined as 'contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent' (Article 8 of ASBE 13 *Contingencies*). This point of view believes that all leases are executory contracts on the grounds that the lessee's right to use the leased property is conditional on paying rentals; and identically, the obligation to make payments is subject to the approval to make use of the property. After that, for the purpose of being consistent with other executory contracts, all of the leases, not just only operating leases under the existing Chinese GAAP, would not be recognized as assets or liabilities by the lessee, instead, information about the lease contracts would be disclosed in the financial statements. Still, leases may not be executory contracts on account of the fact that the lessor has fully performed when possession of the leased assets is transferred to the lessee (Nobes, 2005; Rosenfield, 2006: 493 and 494). The IASB, jointly with the FASB, set up a project in the leasing area, a discussion paper *Leases: Preliminary Views* (the 2009 Lease Discussion Paper) was published in March 2009. As well as its disapproval of the above conceptual flaws in the existing accounting model for leases, the 2009 Lease Discussion Paper commences its criticism first by pointing out the failure to meet the needs of users of financial statements, in particular: (a) users routinely adjust the financial statements of lessees in an attempt to recognize assets and liabilities that are not recognized in operating leases, however, the information in the notes is insufficient for users to make reliable adjustments; (b) the existence of two very different models for leases, which treat similar transactions in distinctly dissimilar ways, reduces comparability for users; (c) the existing standards provide opportunities to structure transactions so as to achieve a particular lease classification, which could be difficult for users to understand (paragraphs 1.12-1.15 of the 2009 Lease Discussion Paper). Following up the above, chapter 3 of the 2009 Lease Discussion Paper advances a right-of-use approach for lessees that would ensure that all assets and liabilities arising under lease contracts are recognised in the statement of financial position. That project is now at the preliminary stage and its final outcome cannot be expected before long yet. An exposure draft that demands a right-of-use model in accounting for all leases (with a few exceptions) was published by the IASB, together with the FASB, in August 2010. In summary, this leases example shows that even if a specific standard in Chinese GAAP is drawn up in accordance with the 2006 Basic Standard, an unsuitable principle may be used; however, it is likely that the 2006 Basic Standard could provide the coming developments with appropriate principles. Anyway, this is just a guesswork made by this writer, since there is no mention of this issue in Chinese GAAP.

There are distinctions between the 2006 Basic Standard and the IASB Framework in some sides, to take an example, both of them discuss faithful representation, but each description of it is dissimilar. In the 2006 Basic Standard, the full terms are as follows: ‘An enterprise shall recognize, measure and report for accounting purposes transactions or events that have actually occurred, to faithfully represent the accounting elements which satisfy recognition and measurement requirements and other relevant information, and ensure the accounting information is true, reliable and complete’ (Article 12 of the 2006 Basic Standard). To draw a comparison, in the IASB Framework, faithful representation, which is a necessary condition of reliability (and substance over form is a necessary condition of faithful representation), is explained as below: ‘To be useful, information must…be reliable. Information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully that which it either purports to represent or could reasonably be expected to represent’ (paragraph 31 of the IASB Framework). ‘If information is to represent faithfully the transactions and other events that it purports to represent, it is necessary that they are accounted for and presented in accordance with their substance and economic reality and not merely their legal form’ (ibid, paragraph 35; note: the phrase ‘economic reality’ does not appear in the preceding citation of Article 16 of the 2006 Basic Standard, which is about substance over form). Besides, for all no reference to faithful representation, the 1992 Basic Standard gives an account of objectivity in the following terms: ‘The accounting records and financial reports must be based on financial and economic transactions as they actually take place, in order to objectively reflect the financial position and operating results of an enterprise’ (Article 10 of the 1992 Basic Standard). From the examination of the previous quotations, it is not difficult to observe that the 1992 Basic Standard solely brings attention to freedom from bias, but is devoid of anything on freedom from error, that could imply that preparers of financial reports might furnish all of users with incorrect information, but it could be assured that no bias is shown in favour of any privileged user group (Xiao and Pan, 1995: 192; 1997). The requirement of objectivity is not set out explicitly any more in the current

Chinese conceptual framework. Although Article 12 of the 2006 Basic Standard use such words as ‘faithfully represent’, it could be deduced that the object after the verb phrase ‘faithfully represent’ should mean ‘Chinese GAAP’, to put it in another way, exactly abiding by Chinese GAAP, which is what companies in China must do, is just the so-called faithful representation. The 2006 Basic Standard gives no further discussion, for example, about what true, reliable and complete information is and how to obtain it; this topic will be continued in the chapter 5. As opposed to the Chinese framework, the IASB Framework states that what to be represented faithfully is ‘that which it purports to represent’. Additionally, section 1 of this chapter explores the notion of representational faithfulness in the US conceptual framework SFAC 2.

Discussions of the concept of faithful representation in all likelihood would relate to whether accounting information can represent faithfully existing underlying economic phenomena, or economic reality, or truth (presuming that they should bear the same essential meaning). Alexander and Archer (2003) examine the ontological and epistemological problems of reality and truth in financial reporting. A description based on that paper can be outlined as follows: On the subject of the ontological issue in accounting, as stated by Searle’s (1995) theory of institutional facts and his concept of collective intentionality, humans have a capacity for sharing intentional states such as belief, desires and intentions. Thus, in addition to the intentional states of individuals, there are shared or collective intentional states, i.e. collective intentionality (Searle, 1995: 23-26). By virtue of collective intentionality, ownership claims, income, and other conceptual objects of accounting can, under appropriate conditions, be institutional facts. (Note that institutional facts can only exist for those who are willing and able to accept the institutions.) Afterwards, though he notes that a socially constructed reality such as money presupposes the existence of a non-socially constructed reality such as metal, paper, electronic records, out of which the former is constructed, Searle (1995: 191-194) believes that social reality, including institutional facts, cannot exist independently of our collective representations of them. Or to say in other words, the view that objects can exist independently of the collective representations may be termed 'external realism', and Searle (op. cit.) rejects an external realism position on social (and economic) reality. Putnam (1981) proposes an alternative ontological basis to external realism, which may be denominated as internal realism. According to internal realism described by Putnam (1981: 49-52), the objects of accounting do not exist independently of a conceptual scheme that relates accounting concepts to each other and to their empirical referents. But this does not mean that such objects are not real. The objects of accounting are part of an economic reality that is socially constructed and objectified by virtue of collective intentionality. By means of the above analyses, Alexander and Archer (2003) assert that external realism is not a suitable ontological theory for accounting or any other discursive practices implicated in the social construction of economic reality, and that internal realism is a suitable alternative. To carry out an exploration of the epistemological issue, to be specific, of how truth in accounting is defined, one among theories of truth is the correspondence theory, which could be exemplified by paragraph 63 of SFAC 2: 'Representational faithfulness is correspondence or agreement between a measure or description and the phenomenon it purports to represent'. And yet, in view of the facts that external realism is not a suitable ontological theory for accounting, and on a normal interpretation a correspondence theory of truth implies external reality, since it implies that there is a reality to which statements correspond if they are true (Searle, 1995: 154), a correspondence theory of truth (as normally interpreted) would be rejected in accounting. Putnam (1981: 49 and 50) raises a different theory of truth, which may be called a coherence theory, as below: Truth, in an internalist view, is some sort of (idealized) rational acceptability, some sort of ideal coherence of our beliefs with each other and with our experiences as those experiences are themselves represented in our belief system, and not correspondence with mind-independent or discourse-independent 'state of affairs'. Alexander and Archer (2003) argue that accounting requires ontological and epistemological theories, to take the examples of internal realism and a coherence theory of truth, that acknowledge the roles of intersubjectivity, collective intentionality and consensus in the construction of social reality and in making judgments about representational faithfulness. Continuing the above arguments, they contend that accounting regulations that take external realism and a correspondence theory of truth as their fundamentals become philosophically problematic. Going further, they find that compliance with GAAP is a necessary, but not a sufficient, condition of providing representational faithfulness. The following footnote [1] is this writer's understanding of Alexander and Archer's (2003) paper, chiefly enlightened by ancient Chinese philosophy.

[1] In ancient Chinese philosophy, there is a very important theory, which was originally put forward by Mencius, one of the two greatest Confucianism founders and Zisi, one of Confucius's students about 2500 years ago, and developed predominantly by Dong Zhongshu (formerly translated as Tung Chung-shu), one of the best-known philosophers in Chinese history about 2200 years ago. It holds that there is a similarity, a uniformity and an integration both between nature's way and human's way and between the world of nature and activities of human. Humans are an integral part of nature, and their physiology, ethic, moral principles, politics and so on are all the direct reflection of nature. Humans are endowed with innate ability and wisdom and should be in full knowledge of nature, and their thoughts should embody nature. Although the harmonization between human and nature is segregated from each other by human's subjective differentiation, it should be naturally fulfilled at last. The above theory has become a branch of the mainstream of Chinese philosophy and exerts far-reaching impact on Chinese thoughts even to date. The previous description is an introduction to the context of harmonization between nature and human. There is another philosophical belief in ancient China, which includes several controversial statements, and the following is a brief account of one of them. As distant as about 2600 years ago, Laozi (also translated as Lao Tzu), one of the most famous philosophers in Chinese history presented an aphorism: The most significant theory is the most simple. Its ground is that the truth has grasped the essence and core of things and can clarify them plainly and vice versa. If the two points above-mentioned are introduced into the field of accounting, a conclusion could be drawn that anything connected with accounting, covering accounting standards, financial statements, accounting literature and things of that description, is created by human. As a result, even if economic phenomena, or to say, the transactions and other events, are numerous and complicated, and the same is true of accounting rules, which also frequently vary according to environmental factors and other influence, the core essence of accounting (could be named X) in human's minds is certainly simple. If it had not been the case, firstly, accounting could not have been created owing to non-existence of such complicated human; secondly, even if it had succeeded, nobody could have both understood and used it, and in the end, accounting would have already vanished for a long time (note: 'simple' signifies by no means that accounting people are simple-minded). Furthermore, there should be a similarity, a uniformity and an integration between accounting's way and human's way as well, to illustrate that, a study of accounting is the study not only of accounting, but also of human, no doubt, including the researcher; the objectives of learning and studying accounting are to attain self-improvement, to enable you to approach as near as possible the core essence of accounting, and to share and discuss the results of your study with other people. The purely philosophical survey of this topic does not fall in the scope of this thesis and this footnote is not its main body either.

(3) Chinese GAAP hierarchy

To revert to conceptual frameworks, the most apparent distinctions between the Chinese conceptual framework and the frameworks of elsewhere probably exist in the following aspect: Article 3 of the 2006 Basic Standard prescribes that 'Accounting Standards for Business Enterprises include the Basic Standard and Specific Standards. Specific Standards shall be formulated in accordance with this [Basic] Standard'. On top of that, the Article 1 of each Specific Standard incorporates such similarities as: In accordance with the Accounting Standards for Business Enterprises: Basic Standard, this [Specific] Standard is formulated to prescribe the recognition, measurement and disclosure of related information of…. The citations above-mentioned imply that Chinese accounting standards totally rest on a conceptual framework, i.e. accounting standards spring from a set of accounting principles; and the conceptual framework is higher than specific standards in the Chinese GAAP hierarchy. These assertions in Chinese GAAP are unique, in contrast with approaches of somewhere else. To give an instance, the IASB Framework explicitly sets forth that it is not an IAS or IFRS, hence does not define standards for any particular measurement or disclosure issue, and does not override any specific IAS or IFRS (paragraph 2 of the IASB Framework); in case of a conflict between the IASB Framework and an IAS, the requirements of the latter prevail (ibid, paragraph 3). Moreover, in the US, its conceptual frameworks, like accounting textbooks, belong to one type of nonauthoritative accounting literature, rather than one part of authoritative US GAAP recognized by the FASB (see Topic 105 *Generally Accepted Accounting Principles* of the FASB Accounting Standards Codification (Codification); at this place one point which is necessary to be expounded is that, since 2004, the FASB had set up a project of developing the Codification, the aim of that project is to integrate and synthesize existing US GAAP in one spot, not to create new GAAP. Since 2009, the Codification has become the single source of authoritative nongovernmental GAAP, and all previous standards established by various standard setters are superseded. The emphasis of this thesis is surrounding the historical process of setting accounting standards, instead of some specifically technical issues, so it does not cite the new Codification, but keep quoting the superseded standards in their primary form). All the same, IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* generally sets down that management is required to consider the applicability of the IASB Framework when there is no relevant standard and interpretation that applies to a specific situation (paragraphs 10 and 11 of IAS 8). None of such provisions is laid down in Chinese GAAP, a presumed understanding of that is that the 2006 Basic Standard itself is a standard, as a consequence, an entity naturally should consider and apply it in the absence of any other specific standards, this view can be supported by Article 2 of the 2006 Basic Standard, which requires that the 2006 Basic Standard shall apply to enterprises established within China; admittedly, the relative Chinese law and accounting practices cannot be in favour of this point. With respect to whether Chinese specific accounting standards are constructed in conformity with the 2006 Basic Standard, all of the illustrations in the preceding parts of this section exemplify the subject, and two more examples will be given in the coming passages.

ASBE 27 *Extraction of Petroleum and Natural Gas* is a new standard promulgated alongside with the 2006 Basic Standard. Chapter 3 of ASBE 27 and Article 2 of the implementation guidance on ASBE 27 specifies that the successful efforts method should be used for the treatment of exploratory drilling costs. Some background information about accounting for oil and gas exploration costs is sketched out below. Amid oil and gas producing activities, companies will expend huge sums of cash on drilling wells in search of commercially viable reserves with the final outcomes ending up either fruitless dry holes or successfully productive wells. Concerning the treatment of exploration costs, one accounting approach is known as the successful efforts method, in which, by and large, only costs relating to successful wells are capitalized and expensed as production proceeds, while costs of dry holes are expensed in the current period. Comparatively, an alternative approach is the full cost method, under which all drilling costs, taking in those incurred in drilling dry holes, are capitalized. Evidently, the amount carried forward as an asset on the balance sheet and the revenue recognition pattern may diverge substantially on the two methods. As to which is the better method, it does not turn out that the definition of an asset in the 2006 Basic Standard (cited on page 82) is helpful in choosing one method over the other. To discuss at length, the reasoning behind the successful efforts method, which is the sole method set out by the Chinese standard ASBE 27, is that a dry hole does not yield future economic benefits, undoubtedly, it will not be able to qualify as an asset. For all that, the asset is actually the oil in the ground, on that account, all the costs of finding the oil, including the costs of dry holes in a portfolio of exploratory drilling, should be capitalized, that means the full cost method is supposed to be accepted (for further elucidation on the full cost versus successful efforts, see Macve, 1983b, in 1997: 219-231). In effect, the instance of oil and gas accounting signals that which is better between capitalization and expensing may not be decided by drawing on the definition of an asset; another example of illustrating this point could be the capitalization issue for research and development costs, which is mentioned in the previous section (page 73; an additional note is that in Chinese GAAP, Chapter 2 of ASBE 6 *Intangible Assets* requires that development costs should be capitalized if certain criteria are met). The history of the oil and gas accounting (note: it would look proper herein to replace 'accounting' with 'political') controversies in the US will be expatiated in the next section. The above cited case denotes that the required accounting treatment in a specific standard could be accounted for by the 2006 Basic Standard, but another alternative method could also be accounted for by the 2006 Basic Standard, even by the identical Article.

And the inability to provide a clarification of the choice between alternatives by using the 2006 Basic Standard is true of accounting for translation of foreign currency transactions, which are those denominated in, or requiring settlement in, a currency other than the enterprise's recording currency (note: 'recording currency' is one of terms in Chinese GAAP and equivalent to 'functional currency' in IASB GAAP). Foreign currency translation denotes the process whereby the entity's financial data expressed in terms of a different currency is restated in terms of the recording currency. Article 11 of ASBE 19 lays down the below requirements, which are essentially in line with the ones in paragraphs 23 and 28 of IAS 21 *The Effects of Changes in Foreign Exchange Rates*: For translation of foreign currency transactions at each balance sheet date, non-monetary items carried at historical cost should be translated using the historical exchange rate prevailing at the date of the transaction, there is no subsequent retranslation; and monetary items such as receivables and payables should be translated into the recording currency at the closing rate, i.e. the spot exchange rate as of the balance sheet date; exchange differences arising on translating monetary items at rates different from those at which they were previously translated should be recognized in profit or loss in the period in which they arise. Arguably, the above illustrations could be counted that method of translating monetary items at the closing rate set out in ASBE 19 is founded on the accrual basis of accounting set forth in Article 9 of the 2006 Basic Standard. To put it concretely, the change in exchange rates occurs during the current period, in consequence of that, the current value of monetary items expressed in the recording currency should be accordingly recognized and the translation difference should be taken as a gain or loss for the current period, as opposed to waiting until the future period when the monetary asset or liability will be liquidated. However, Article 18 of the 2006 Basic Standard prescribes that 'an enterprise shall exercise prudence in recognition, measurement and reporting of transactions or events. It shall not overstate assets or income nor understate liabilities or expenses'. Could the prudence principle be followed, monetary assets would be translated at the lower of the historical rate and the closing rate, since a future change in exchange rates may well cancel out a gain made in the current period and consequently it would be imprudent to report any gain that is unrealized. For the same reason, monetary and non-monetary liabilities would be stated at the higher of two possible values (for explication at great length about foreign currency transaction, look at Flower, 2004a). As noted in the cases of both oil and gas exploration and translation of transactions, the accounting method existing in a specific standard could be thought of being formed in conformity with the 2006 Basic Standard, and yet alternative possible accounting practices could have their origin from the 2006 Basic Standard the same way; but, above all, as illustrated in all of the previous instances in this section, Chinese specific standards give no elucidation of the stipulated methods whatsoever.

(4) a brief summary

By means of exemplification of typical cases, this section discusses the contents of Chinese conceptual framework, namely, the 2006 Basic Standard; and simultaneously, contrasts, both in substance and in form, the similarities and differences between Chinese and IASB GAAP. Through the analyses of the illustrations in this section, this writer's view is that the provisions presented in the 2006 Basic Standard could clarify the modifications to specific standards of both deferred taxes and inventories cost formulas, could hardly define accounting treatments for construction contracts and government grants, could describe both the existed and the proposed accounting models for leases, and could justify both the allowable and the prohibitive approaches in accounting for oil and gas exploration costs and translation of foreign currency transactions. According to those discussion and exploration, the conclusion of this section is that: in spite of some dissimilarities in certain aspects, the terms of the 2006 Basic Standard are basically similar to the ones of the IASB Framework; in spite of Chinese GAAP's claims that specific accounting standards are formulated in accordance with the 2006 Basic Standard, not only does the 2006 Basic Standard merely touch upon or solely list accounting principles and conventions without any further going into details, for example, how to apply them to spell out the specific standards, but also these specific standards never give any indication of how they are based on the 2006 Basic Standard. The previous three sections of this chapter chiefly make analyses and comparisons of most parts between the Chinese and international conceptual frameworks, this section also alludes to one of the functions of a conceptual framework, which Chinese GAAP asserts is the basis of accounting standards. The next chapter will detail the roles of conceptual frameworks.

V A DISCUSSION OF THE ROLE OF CONCEPTUAL FRAMEWORKS

1. two examples

(1) accounting for pensions

First of all, to take two examples as help with clarification of what functions conceptual frameworks could serve, which is the theme of this chapter. The first one is from accounting for defined benefit pension plans. Under defined benefit plans, the amount of pension benefits that the enterprise promises to provide its retirees with is prearranged, that means that the enterprise bears the risk of pension fund performance; in regard to the accounting treatment, actuarial assumptions, including demographic and financial estimates, are required to measure the defined benefit obligation and the expense, hence a possibility of actuarial gains and losses, which somewhat implies the difference between the actuary's current estimation of the fund and obligation. The US standard SFAS 87 *Employers' Accounting for Pensions* does not permit immediate recognition of actuarial gains and losses; instead, adopts a 'corridor' approach: differences less than 10 percent of the present value of the obligation (or the fair value of the plan asset if it is greater) are ignored, and the excess is amortized systematically (paragraphs 29-33 of SFAS 87). Large numbers of accounting academics (e.g. Schuetze, 1991, in 2004: 48; Nobes, 2005) hold their view that the 10 percent thresholds rule is an income (or volatility) smoothing device and is not consistent with conceptual frameworks; moreover, they advocate full and immediate recognition of actuarial gains and losses, for that approach satisfies the definition and recognition criteria of a liability drawn up in SFAC 6. Nevertheless, the standard SFAS 87 presents its below description, which is extracted from paragraphs 173-190 of Basis for Conclusions, under the subheading 'Volatility and Delayed Recognition of

Gains and Losses': 'The [FAS]Board does not believe that reporting volatility per se is undesirable. If a financial measure purports to represent a phenomenon that is volatile, the measure must show that volatility or it will not be representationally faithful' (paragraph 174 of SFAS 87). 'However, in the case of pension liabilities, volatility may not be entirely a faithful representation of changes in the status of the obligation (the phenomenon represented)' (ibid, paragraph 175). After 'the [FAS]Board' considered a few respondents' views and suggestions (see ibid, paragraphs 176-186), '[t]he [FAS]Board was attracted to the 'corridor' approach required by this Statement[FAS 87] as a minimum amortization approach in part because it allows a reasonable opportunity for gains and losses to offset each other without affecting net periodic pension cost' (ibid, paragraph 187). Quite evidently, at least two points can be assumed from the wording of SFAS 87 above quoted: firstly, 'the [FAS]Board's opinions' always prevail, secondly, the FASB is of the opinion that the corridor requirement in SFAS 87 does not violate principles established in conceptual frameworks, or even is squared with the principle of representational faithfulness (expounded in paragraphs 63-71 of SFAC 2). Undoubtedly, there is very little likelihood of the above two points being not contentious.

IASB GAAP for pension plans is advanced in IAS 19 *Employee Benefits*, which allows not only the 'corridor' treatment, i.e. recognizing nothing inside a 10 percent corridor and amortizing the amount outside the corridor over the average remaining service lives of employees; but also a faster, or even immediate, recognition of (the entire) actuarial gains and losses as income or expense; or a full recognition of actuarial gains and losses to the statement of changes in equity (paragraphs 92-95 of IAS 19). It is obvious that choices between alternative methods permitted by IAS 19 would impair comparability, which is a principal qualitative characteristic and raised in paragraphs 39-42 of the IASB Framework; moreover, fundamentally speaking, only if the whole actuarial gains and losses is immediately recognised in the income statement, could this method be consistent with the definitions of the elements of financial statements described in paragraphs 47-80 of the IASB Framework. The aforementioned can be read in paragraphs 48K and 48L of Basis for Conclusions of IAS 19; and yet, at the same time, that Basis for Conclusions propounds the following exposition of the IASB's reasons for the selection of alternative solutions: 'The [IAS]Board considered five methods of accounting for actuarial gains and losses…' (paragraph 38 of Basis for Conclusions, IAS 19). 'Arguments for [a deferred recognition] approach are that: …[The volatility in liability and expense] may not be a faithful representation of changes in the obligation… and in the long term, actuarial gains and losses may offset one another…' (ibid, paragraph 39). 'Arguments for an immediate recognition approach are that: … It represents faithfully the entity's financial position…; a financial measure should be volatile if it purports to represent faithfully transactions and other events that are themselves volatile…' (ibid, paragraph 40). 'The [IAS]Board found the immediate recognition approach attractive. However, the [IAS]Board believes that it is not feasible to use this approach for actuarial gains and losses until the [IAS]Board resolves substantial issues about performance reporting…' (ibid, paragraph 41). 'Arguments for [a corridor approach] are that they…represent faithfully transactions and other events that are themselves volatile…' (ibid, paragraph 42). 'The width of a 'corridor' is arbitrary. To enhance comparability, the [IAS]Board decided that the width of the 'corridor' should be consistent with the current requirement in those countries that have already adopted a 'corridor' approach, notably the [US]' (ibid, paragraph 48). From the above quotation, it is observable that opposite positioned commentators cite the identical principle in the IASB Framework, namely faithful representation (laid down in paragraphs 33-35 of the IASB Framework), as essentials to underpin their preferences. What is more, despite its acknowledgement that permission for multiple options hinders comparability, the IASB keeps use of the principle of comparability to uphold one sort of the prescribed accounting treatments in IAS 19. In addition, although it finds the immediate recognition approach more appealing from a conceptual perspective, the IASB further places its preponderance both on the need for the practicalities of accounting treatments for post-employment benefits and on the lack of theories about reporting comprehensive income, therefore the application of the immediate recognition method is still premature (paragraphs 46 and 48K of Basis for Conclusions, IAS 19).

In summary, although IAS 19 in international GAAP does not restrict the recognition of actuarial gains and losses to the corridor and deferring approach derived from SFAS 87 in US GAAP, and the two standards seemingly take conceptual frameworks into consideration likewise, in reality, what both of them primarily consider could be management's concerns such as averting (over) volatility in accounts, which is not a principle in any conceptual framework. Manifestly, both the US conceptual frameworks and the IASB Framework declare that the objective of financial reporting is decision usefulness (paragraph 34 of SFAC 1; paragraph 12 of the IASB Framework); some financial analysts, who could be advisers of investors, propose that providing a pension standard could furnish information that is useful in making economic decisions, it is supposed to prescribe that deferrals of actuarial gains and losses should be included in the pension expense, and the difference between plan assets at fair value and the benefit obligation (including an estimate of future increases in salary) should be recognized on the balance sheet, known as the funded status, for that method more accurately reflects the underlying current economic situation of a company (see Wild et al., 2003: 151-155). Regardless of its claim that the basis for its provisions is derived from conceptual frameworks, SFAS 87 is almost unanimously perceived as a rules-based standard; AAA's FASC (2003) presents a reformulated SFAS 87 that rests on the FASB's conceptual frameworks and scraps the corridor rule. In 2006, the FASB issued SFAS 158 *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans: an amendment of FASB Statements No. 87, 88, 106, and 132(R)*, which requires that the funded status of a benefit plan should be recognized on the balance sheet rather than in the notes, and all transactions and events affecting that funded status be recognized through comprehensive income in the year in which they occur. Chinese GAAP does not approach the accounting requirements for defined benefit plans (perhaps being devoid of such postemployment benefits in China). Taking the above case of pension accounting is in an attempt to examine the use of conceptual frameworks in rules-based standards; with reference to principles-based standards, business combination accounting could be another typical example.

(2) business combinations

In US GAAP, before the implementation of the existing standards SFAS 141 *Business Combinations* and SFAS 142 *Goodwill and Other Intangible Assets,* the accounting treatments for mergers and acquisitions were given in APB Opinion 16 *Business Combinations* and APB Opinion 17 *Intangible Assets*, which recognize two distinct methods of accounting for business combinations, that is, the purchase method and the pooling of interests method. The purchase method accounts for a business combination as the acquisition of one company by another. Under the purchase method, companies are required to recognize the fair values of assets and liabilities acquired in the consolidated balance sheet; a difference between the cost of an acquired company and the sum of fair values of net assets is recorded as goodwill and amortized over a period not to exceed 40 years. In contrast, the pooling of interests method accounts for a business combination as the uniting of the ownership interests of two or more companies by exchange of equity securities. Under the pooling method, a consolidated balance sheet just combines existing balance sheets; assets and liabilities of separate entities are carried forward at their book values, and thus no goodwill is recognized. By contrast with the purchase method, the pooling method could have certain attractiveness to the management, including low (reported) asset amounts and high (reported) income; in particular, the avoidance of goodwill means that the subsequent earnings reduction resulting from goodwill amortization would be avoided. Two other causes of reporting more net income under the pooling method are that: First, depreciation is only computed on the book values of both companies, not on the fair values (of the acquired assets), and in periods of rising prices, the book values of fixed assets tend to be lower than the fair values, therefore, the depreciation of lower carrying amounts means that net income is higher. Second, the consolidated income statement includes the income statements of both companies for the entire fiscal period in which the combination occurs rather than subsequent to the acquisition date (some detailed rules are as follows: paragraph 11 of APB Opinion 16 specifies that in a purchase, the reported income of an acquiring corporation includes the operations of the acquired company after acquisition, based on the cost to the acquiring corporation; paragraph 12 of APB Opinion 16 demands that in a pooling, income of the combined corporation includes income of the constituents for the entire fiscal period in which the combination occurs). However, paragraphs B36-B79 of SFAS 141 detail the demerits of the pooling method, which, as an illustration, records the combination in terms of the carrying amounts of the parties to the transaction, hence its failure to reflect the investment made in the combination and to hold management accountable for that investment and its subsequent performance (paragraph B57 of SFAS 141); on that account, the FASB abolished the pooling method for any business combination in SFAS 141. In academic studies, as expected, some researchers suggest that share prices depend on the choice between purchase and pooling method; conversely, other ones conclude that accounting does not matter. For instance, Hopkins et al. (2000) design an experiment, which is generally such a job: letting investment analysts estimate a company's share prices separately under the purchase method and the pooling method. Their experimentation concludes empirically that analysts' share price judgments depend on the method of accounting for a business combination as well as the number of years that have elapsed since the combination. To go into details, when a company applies the purchase method and rateably amortizes goodwill, the share price projected by the analysts is the lowest; and yet, when a company uses the purchase method and writes off the acquisition premium as in-process research and development, analysts' share price judgments are not statistically different from their judgments applicable to a company applying the pooling method. As well as demonstrating Hopkins et al.'s (2000) own research, that paper reviews more than ten databases archival literature on the relation between business combination accounting and share prices, the fact turns to be that no clear pattern is emerged from those prior studies; certainly, the conclusions drawn by Hopkins et al. (2000) cannot apply universally either. In other words, researches that seek an answer to a posed question through quantitative means, or known as positive accounting research, do not bring scientific and trusted conclusions on the subject of the effect of business combination accounting on share price, and naturally do not clarify which one is better between purchase and pooling accounting. Chapter 8 will continue the discussion about the topic of positive accounting research.

SFAS 141, which became effective from 1 July 2001, requires that all business combinations, except for those involving not-for-profit entities and combinations of entities under common control, must be accounted for as purchases (paragraph 13 of SFAS 141). As above-mentioned, SFAS 141 is typical of principles-based standard (e.g. in the SEC Report); concerning this view of point, the finest expression of SFAS 141 as a principles-based standard is almost certainly in the standard itself. By way of illustration, SFAS 141 includes a section entitled 'How the Conclusions in This Statement Relate to the Conceptual Framework'; brief excerpts from that section are given below: 'The [FAS]Board concluded that because virtually all business combinations are acquisitions, requiring one method of accounting for economically similar transactions is consistent with the concepts of representational faithfulness and comparability as discussed in [SFAC 2]. The [FAS]Board also noted that [SFAC 1] states that financial reporting should provide information that helps in assessing the amounts, timing, and uncertainty of prospective net cash inflows to an entity. The [FAS]Board noted that because the purchase method records the net assets acquired in a business combination at their fair values, the information provided by that method is more useful in assessing the cash-generating abilities of the net assets acquired than the information provided by the pooling method. [SFAC 2] states that a necessary and important characteristic of accounting information is neutrality…. The [FAS]Board concluded that its public policy goal is to issue accounting standards that result in neutral and representationally faithful financial information and that eliminating the pooling method is consistent with that goal' (pages 7 and 8 of SFAS 141). The above quotations make it pretty convincing that SFAS 141 is principles-based. Nevertheless, Benston et al. (2006) argue that the purchase method results in combining together the estimated market values of the acquired assets and liabilities with the historical book values of the acquirer's assets and liabilities, consequently, they ask what the sum of these numbers means in terms of 'representational faithfulness' principle. In addition, the purchase method is not without defects in practice, for example, as indicated in Hopkins et al. (2000), companies could write off a significant portion of the acquisition costs as acquired in-process research and development on the acquisition date, thereby reducing or eliminating goodwill amortization in later years, and improving return on equity or return on assets measures due to increase in the numerators and decrease in the denominators (the relative context is as follows: US GAAP on in-process research and development is set out in FASB Interpretation 4 *Applicability of FASB Statement 2 to Purchase Business Combinations*, which generally requires that the fair value of acquired in-process research and development be immediately expensed. However, there are no rules about how to assess in-process research and development before writing them off. SFASs 141 and 142 do not specify this aspect).

With respect to the formulation of SFAS 141, the standard itself describes the process as: taking the 'Reasons for Rejecting the Pooling Method' section as an example, 'Some proponents of the pooling method argued that the information it provides for some business combinations is more decision useful…' (paragraph B43 of SFAS 141). 'The [FAS]Board observed that an important facet of decision-useful information is information about cash-generating abilities and cash flows generated[, as stated in SFAC 1]. ...Because the pooling method records the net assets acquired at their carrying amounts rather than at their fair values, the information that the pooling method provides about the cash-generating abilities of those net assets is less useful than that provided by other methods' (ibid, paragraph B44). 'The [FAS]Board also concluded that the information provided by the pooling method is less relevant in terms of completeness, predictive value, and feedback value than the information that is provided by other methods' (ibid, paragraph B45). 'Comparability is another important facet of information that is decision useful[, as stated in SFAC 2]. 'After considering all of the views expressed by respondents, the [FAS]Board agreed with those that stated that comparability of financial information reported by entities that engage in business combinations would be enhanced by eliminating the pooling method' (ibid, paragraph B50). 'A number of respondents…argued that public policy considerations [such as the development of new technology and entrepreneurial culture] should dominate the [FAS]Board's decisions' (ibid, paragraph B69). 'The [FAS]Board noted that [paragraph 98 of SFAC 2] states that neutrality means that either in formulating or implementing standards, the primary concern should be the relevance and reliability of the information that results, not the effect that the new rule may have on a particular interest' (ibid, paragraph B72). 'The information provided by those respondents did not cause the [FAS]Board to change its view that its public policy goal is to issue accounting standards that result in neutral and representationally faithful financial information and that eliminating the pooling method is consistent with that goal' (ibid, paragraph B76). The presentation of SFAS 141 suggests quite strongly that it is principles that make the pooling method rejected and SFAS 141 formulated by the FASB. – With the caveat that it may not be 'representational faithfulness'.

Looking back on historical events, the FASB's predecessor, the APB, once made an effort aimed at removing the pooling alternative as early as the late 1960s, long before the formulation of conceptual frameworks and the FASB's 1999 exposure draft *Business Combinations and Intangible Assets* (the FASB 1999 Business Combinations Exposure Draft), which, in reality, tried a second time in history to eliminate the pooling method. However, owing to a lack of support from the SEC and the management, not only did the accounting standard APB16 issued in 1970 fail to prohibit the pooling method, but also the accounting standard setting body the APB failed to exist, and it was replaced by the FASB in 1973 (see Rosenfield, 2006: 463 and 464). Essentially, the US standard setting process is highly politicised, and to a greater degree, that is contributed to the fact that the FASB's authority for setting standards is derived primarily from the SEC, and the SEC derives its authority from the US Congress (and the US president, who has the presidential veto). The general background information is as follows: The SEC, an independent government agency, was established by Congress in 1934 to administer the Securities Act of 1933, the Securities Exchange Act of 1934 and several other regulations. In its Accounting Series Release 150 of 1973, the SEC officially affirmed that the task of setting accounting standards has been delegated to the FASB, an organization in the private sector. Concurrently, the SEC retains its authority for enforcement, along with imposing its own rules or overriding the FASB's standards. Hence the FASB's authority and its existence primarily count on the endorsements of its standards by the SEC; likewise, Congress, which holds the ultimate power, can ultimately threaten the survival of the SEC, let alone the FASB. Consequently, apart from participating in the FASB's due process, groups who may be affected by a proposed FASB standard can also lobby the SEC and Congress to exert pressure on the FASB to compromise, or directly intervene in particular accounting matters. Finally, it is expected that the FASB has to acknowledge the supreme authority of Congress and the SEC, and fulfil their requirements, which most likely reflect the demands of those involved lobby groups (see Miller et al., 1994: 19-22, 148-151). This is politics indeed.

This paragraph is based on Beresford (who used to be the chairman of the FASB)'s (2001) paper. By reason of the power structure outlined above, a Congressional hearing is a very strong form of political involvement in setting accounting standards. Congressional hearings are infrequent, but they are bound to be taken very seriously by the FASB, whose position is usually the target of attack in those hearings. The case of business combinations clearly highlights this point. At the Senate hearing in March 2000, the panel which was composed of prominent figures of large companies (such as a certain well-known venture capitalist who made his investment mostly in the new economy, chief executive officer (CEO) of American Express, and vice president of Cisco Systems) made a politically stimulating appeal for saving the US economy, as they were concerned that the prohibition of the pooling method could lead to significant adverse consequences, including slowing economic growth and job creation, undermining global competitive strength, constraining technological innovation, and so on. Similar apprehension over stifling growth of the US (new) economy was also expressed in the succeeding House hearing by both Representatives and corporate delegates, including the one from Cisco Systems at the previous hearing (Cisco noticeably used pooling accounting for several very large acquisitions). At both the Congressional hearings, the FASB responded by pointing out that the purchase method can provide much more relevant information about business combinations compared to allowing alternative methods, and by reiterating the FASB's commitment to its independence and neutrality in standard setting. Additionally, in October 2000, a bill trying to postpone eliminating the pooling method was introduced in the House of Representatives. More specifically, a Representative brought forward a bill, Financial Accounting for Intangibles Reexamination (the abbreviation for politically agitating FAIR) Act, which mainly requires establishing a Federal Commission on Financial Accounting for Intangibles to study the accounting for business combinations and intangibles and to consider the economic impact that will result in if poolings are eliminated. If that bill had been enacted, not only might the pooling method have been retained, but also the FASB's status as the primary standard setting body might have been challenged (The above content is seen in Beresford (2001); besides, that FAIR Act was eventually opposed). With respect to supporters of the FASB, Financial Executives Institute (FEI), members of which are primarily corporate accounting officers at highest levels, and Institute of Management Accountants (IMA), which consists mainly of corporate accountants at all levels, are two of the eight sponsoring organizations that have special powers in the governance of the Financial Accounting Foundation (FAF), which oversees operations of the FASB. That is to say, these two nongovernmental bodies have a crucial role in establishing the authority of the FASB (see Miller et al., 1994: 23). Both the FEI and the IMA sent letters to Senators and Representatives to defend the FASB's due process and the importance of the standards setting's independence from government. Furthermore, in a letter replying to a Representative about its role for the FASB's agenda in May 2000, the SEC emphasized that it supervises rather than dictates the standard setting process. Subsequently, the SEC confirmed that it would not override the FASB's business combinations project (summarized in Beresford, 2001). It is time to count votes. The FASB had the support of the SEC and accounting professional organizations, but faced opposition from the business community and some members of Congress. Though there might be no one-to-one causal relationship, the history was that the pooling method was eliminated, but the accounting rule for goodwill changed from amortization to impairment. Anyway, rest assured, the standard SFAS 141 does not say a single word whatsoever about the above stated political intervention amid the process of the standard setting.

Initially, the FASB 1999 Business Combinations Exposure Draft requires that purchased goodwill is amortized over no more than 20 years (40 years in APB Opinion 17); following Congressional hearings, the FASB commenced discussing with business representatives a proposed impairment test applying a present value technique to account for goodwill; and the final standard SFAS 142 demands that goodwill is no longer amortized, but should be tested at least annually for impairment and any loss is reported in the income statement (paragraphs 18-22 of SFAS 142). The FASB's own account of the cause and process of redeliberating accounting for goodwill can be seen in paragraphs B79-B100 of SFAS 142, and the FASB concludes that nonamortization of goodwill coupled with impairment testing is consistent with the concept of representational faithfulness (page 7 of SFAS 142). The standard setter FASB is of the opinion that the accounting for goodwill is principles-based, however, just as Beresford (2001) indicated, presumably the requirements of impairment tests are also for the sake of easing the management's fears about large future earnings reduction caused by goodwill amortization. In addition, Rosenfield (2006: 468-471) argues that it is impossible to carry out a satisfactory test for the impairment of goodwill, which is immeasurable pure prospects; and he suggests that the amount of goodwill related to business combinations should be immediately charged to income at the date of acquisition. By critically reviewing the FASB's definition of an asset (mentioned on page 70), Schuetze (2001, in 2004: 160-162) also concludes that goodwill is not an asset, but should be charged to expense mainly because it cannot be converted to cash. Many accounting academics (including Rosenfield and Schuetze, op. cit.) advocate fresh start accounting, which treats the business combination as creating a new entity, therefore requires revaluation of all the assets of the combining entities at current value at the date of the combination. The FASB, together with the IASB, has set up a project to consider the application of the fresh start approach to circumstances where an acquirer cannot be identified in a combination, yet the outcome of the project will not be produced in the near future. Only in passing, IASB GAAP prohibits the pooling method in IFRS 3, which superseded IAS 22 *Business Combinations* (poolings allowed) with effect from 31 March 2004. This change noticeably came under the influence of the new US requirements in SFAS 141 rather than the IASB Framework, which had been published for more than ten years. The Chinese standard ASBE 20 provides that the pooling of interests method should be used for business combinations involving entities under common control (Chapter 2 of ASBE 20), the other business combinations should be accounted for as purchases (Chapter 3 of ASBE 20), and the goodwill should be tested for impairment in accordance with Chapter 6 of ASBE 8. At this place one matter may need to be made clear that the former US standard APB Opinion 16 does not allow companies' free option of the use of purchase or pooling accounting. In effect, the pooling method is only applied to business combinations involving the exchange of equity securities (paragraph 12 of APB Opinion 16); furthermore, paragraphs 46-48 of APB Opinion 16 put forward twelve specific conditions, all of which must be met for a business combination to be classified as a pooling of interests. But as stated above, in practice, on that account that the pooling method can provide certain benefits to the merged enterprise, companies that otherwise would be expected to use purchase accounting turned out to be willing to incur significant direct and indirect costs to qualify for pooling treatment. Coming back to combinations of entities under common control, they could be perceived as mergers of parent and subsidiary or of two subsidiaries, the current US standard SFAS 141 clarifies that itself does not involve this kind of combinations, the relative discussion is chiefly brought up in Issue 02-5 *Definition of 'Common Control' in Relation to FASB Statement No. 141*, which is presented by the Emerging Issues Task Force (EITF, created by the FASB), and together with the other pronouncements in US GAAP, prescribes that mergers among affiliated entities should be treated by a method essentially identical to pooling of interests accounting. Incidentally, there is a Chinese peculiarity which needs noticing that a huge number of enterprises in China are state-owned, hence a possibility that the merger partners would found a parent corporation in advance, as a result, the pooling method for that combination could be applied. Certainly, that is just a deduction.

To sum up, the above exemplification of post-employment benefits and business combinations demonstrates an idea that we may need to distinguish between accounting standards and accounting standards setting (this point was mentioned at the beginning of chapter 4). Firstly, any standard could be interpreted as applying some principles, for the underlying reason that, on the one hand, conceptual frameworks are thought to be incomplete, internally inconsistent, and ambiguous (could be seen in chapter 4), moreover on the other hand, any involved parties are able to provide their own descriptions of the relation between an accounting treatment and accounting principles, however some of the descriptions may not be intellectually honest such as the ones from the management. Secondly, even though the standard is principles-based, the process of standard setting is prone to be politicized, predominantly because of the management's involvement in it (see Solomons, 1978); there is no connection at all between the discourse embraced in the linguistic system employed by the politicized process and accounting principles encompassed in a conceptual framework. With regard to the differentiation between principles-based and rules-based accounting standards as mentioned above, a brief account of background information is as follows: In consequence of the Enron and other business scandals, the public, in particular investors, called for actions taken by the US government; in response to that, Congress passed the Sarbanes-Oxley Act of 2002 (named after its principal sponsors), which tries to reform the financial reporting system in the US. Largely because of the fact that Enron, with the assistance of its external auditor, produced seriously misleading financial statements that ostensibly met the technical requirements of US GAAP, but effectively violated its intent, the Sarbanes-Oxley Act instructed the SEC to conduct an investigation into whether the US should adopt a principles-based accounting system; in accordance with the Act, the SEC Report (introduced on page 78) was published in 2003. The SEC Report rejects rules-based standards, because that sort of standards can provide a roadmap to avoidance of the accounting objectives inherent in the standards, and result in financial reporting that is not representationally faithful to the underlying economic substance of transactions and events. Meanwhile, the SEC Report also rejects principles-only standards, partly because it would provide insufficient guidance to preparers and auditors in the application of the principles, hence a loss of comparability. Consequently, the SEC Report proposes a principles-based approach, which is termed objectives-oriented standard setting in order to differentiate the SEC's perception of principles-based approach from those suggested by others. According to the SEC Report, principles-based (or objectives-oriented) standards should involve a concise statement of substantive accounting principle where the accounting objective has been incorporated as an integral part of the standard, provide an appropriate amount of implementation guidance given the nature of the class of transactions or events, and be consistent with, and derive from, a coherent conceptual framework of financial reporting. Nevertheless, the SEC Report fails to make it clear what 'an appropriate amount', 'a coherent conceptual framework' etc are, in other words, the concept of objectives-oriented standards does not be explicitly defined. Reverting to the issue of principles-based versus rules-based accounting standards, the debate over that issue has yet to come up with a result, the difficulty in furnishing accurate definitions of principles-based and rules-based can hardly be the only reason, in fact, the different individual interests harboured by different players who take part in the debate could be the essential reason (see Alexander and Jermakowicz, 2006 for details). One point could be noticed that from the perspective of accounting standard itself (that is, without any outside influence), none of accounting standards can be formulated merely by drawing on the 'principle', namely the general 'principle' which exists in a person's mind. Instead, standards should be written out after standard setters have taken into consideration one or more specific lower-level principles such as the definition of an element, matching concept and so on incorporated in a general higher-level 'principle', therefore, the view of point that the US rules are often based on principles advanced by Schipper (2003; note: she was a member of the FASB at the time, certainly the usual caveat applies) appears reasonable; but yet, the one or more specific lower-level principles above-mentioned are probably deemed as inappropriate by someone else, so the opinion that the need for rules is caused by a lack of appropriate principles put forward by Nobes (2005) also seems justifiable. Or, in other words, accounting standards should fundamentally originate from the core essence of accounting, which could be named as an X, but are unable to thoroughly reflect or disclose the core essence of accounting, because no X-only accounting standards can be written out, any standard may only be an approximation of that X. Anyway, whether accounting standards are principles-based or rules-based is not able to alter the reality that the formulation of accounting standards is intervened by the management and other interested groups. The case of accounting for business combinations generally culminated in the FASB's win, two more illustrations of accounting standards setting are provided below.

2. oil and gas accounting and share options

The first one is previously mentioned in the section 3 of last chapter and concerned with the debate over the oil and gas accounting, the following is a brief historical review: Since the 1950s, smaller and newer oil companies had generally adopted the full cost method, whereas larger companies normally used successful efforts; and no oil and gas accounting project was included on the FASB's initial agenda. However, during the 1970s, in consequence of a war in the Middle East and an embargo of their oil to the US by the Organization of Petroleum Exporting Countries (an international oil cartel, also known as OPEC), the price of oil skyrocketed. Because of that, energy policy became a matter of supreme national significance in the US; one of its essential points was that the government demanded reliable and comparable data on the size and the costs of oil and gas reserves. Under the Energy Policy and Conservation Act of 1975, there were a number of requirements, one of which was that Congress charged the SEC with establishing the appropriate (and uniform) oil and gas accounting rules; the SEC turned to the FASB for developing the relevant accounting standard. The outcome was the release of SFAS 19 *Financial Accounting and Reporting by Oil and Gas Producing Companies* in 1977, which required the use of successful efforts only and outlawed full cost. This selection appalled a great number of smaller oil companies adopting the full cost method, as they were worried that the application of the new standard SFAS 19 would decrease their asset values and shareholders' equity, accordingly, could cause problems involving existing accounting ratios-based debt contracts, and could frustrate their opportunities to raise capital. Moreover, supporters of full cost were also concerned that switching to successful efforts might depress their future profits, and thus affect management bonuses decided by profits. As opposed to the above, larger oil firms already using successful efforts might be suspected that they favoured one kind of more conservative approach so as to diminish political risks brought about by high profits, such as further regulation of prices or windfall taxes. Having learnt about the backing from the SEC for the FASB, the full cost lobby launched a sweeping campaign, including appeals to the Department of Energy, to the Department of Justice (for the reason that SFAS 19 might bias towards big companies), to Congress and so forth. Under political pressure, the FASB held a series of public hearings (which were not well attended); following that, in 1978, the SEC rejected SFAS 19 before it became effective and allowed the continued use of both the successful efforts and full cost methods. Necessarily, in 1979, the FASB likewise issued SFAS 25 *Suspension of Certain Accounting Requirements for Oil and Gas Producing Companies: an amendment of SFAS No. 19*, confirming that both methods were acceptable. At the same time, the SEC imposed a new requirement, that is, reserve recognition accounting, which looks on net income figure for a year as the increase in the value of newly discovered reserves, plus the changes in the value of previously discovered reserves over that year, both being measured at current values; in other words, reserve recognition accounting avoids the capitalization versus expensing controversy under the historical cost basis, as all drilling costs will be reported on the income statement in the year they are incurred. However, this method would recognize income exactly at the time when oil is discovered and along with constant fluctuations in oil prices rather than waiting until the oil is actually sold, and would entail estimating future cash flows and employing the present value measurement technique, therefore it would involve the assessment of several highly uncertain engineering and economic factors, for example, the physical quantity of the reserves, the future time to extract them, the then prices, and so on. The SEC intended to make reserve recognition accounting, which arguably could offer users more relevant information about an oil company (for physical estimates of reserves are crucial information in assessing share values of oil companies), become the primary basis of reporting by oil and gas producers; but the whole oil industry and auditors opposed the SEC's plan on the grounds that the uncertainty brought in made the reliable measurement of the value of reserves unfeasible. Probably owing to that opposition and a precipitous plunge in oil prices, or more possibly, because a new president, who advocated reducing the burdens of federal regulations, took office, the importance of energy policy petered out, and the SEC dropped its plan to make reserve recognition accounting mandatory in 1981. In the coming year, with the support of the SEC, the FASB issued SFAS 69 *Disclosures about Oil and Gas Producing Activities*, which supersedes SFASs 19 and 25, and accepts both full cost and successful efforts, and at the same time provides that companies should supply supplementary information similar to what would be generated by reserve recognition accounting (arguably oil and gas accounting was back to square one; the historical review and discussion on this topic can be seen in Macve, 1983b, in 1997: 219-231; Miller et al., 1994: 120-122). The above case illustrates that in the formulation of the oil and gas accounting rules, the government (including Congress), the SEC, smaller oil companies, larger oil companies, auditors, and the FASB were all involved; these individuals and groups possessed their own intentions, and certainly, only were they most clear about what they wanted to gain. Zeff (1978) calls this fact that one accounting policy can exert distinct impact on the decision making of different parties as 'economic consequences'. It is commonly thought of that the FASB attempted to make authorities believe its competence in acting as a private sector professional accounting standard setting body; the FASB (and its predecessor, the APB) had been often criticised for its use of the ad hoc approach instead of fundamental principles to deal with particular problems, and consequently, the FASB's conceptual framework project could be viewed as the effort in searching for accounting principles (Macve, 1983a, in 1997: 167-217). On the publication of SFAS 19, the FASB had not formed a conceptual framework, the following is an instance after the existence of conceptual frameworks.

Although transferring cash is the most common way an entity pays for the employee services, it is not the sole one; share options are also a common feature of employee remuneration. These options grant executives and other employees rights to buy the entity's shares at a fixed price for a specified period of time, and the exercise price of the option tends to be less than the market price as of the exercise date. Since share options can pay salaries as a substitute for cash, enterprises with a scarcity of cash, e.g. many small high-tech companies, normally furnish their employees with a large quantity of options; at the same time, these options offer management and other employees a chance of participating in the capital growth of the company, and arguably make the objectives of management and shareholders congruent. Originally, US GAAP on employee share options was set out in APB Opinion 25 *Accounting for Stock Issued to Employees* (note: 'stock' is the US term for shares; this paragraph uses the IASB term 'shares'), which was published in 1972 and effectively required that no compensation expense for the options was recognized. More specifically, APB Opinion 25 adopts the intrinsic value method, under which the cost of conferring share options on employees is limited to the excess of the market price of the share at the grant date over the exercise price of the option, namely the intrinsic value (at the date of grant); as the exercise price is typically fixed above the market price at the grant date, the compensation charge is rarely to be recognized (note: intrinsic value can never be negative, it is simply zero). The method of bypassing the income statement could be derived from the argument that even if the options are finally exercised, share-based compensation arrangements do not ever cost the entity any cash or other resources, therefore no expense is incurred at any time. Nevertheless this judgment should be false, because compensation associated with employee share options is representative of a component of a remuneration package that is a payment in consideration of services received by the entity, so share options are certain to hold value (otherwise executives would not have sought to gain them as many as possible), consequently, like other labour costs, the value of share options is supposed to be expensed over the period during which employees are earning the options. Moreover, as far as existing shareholders are concerned, since nearly none of compensation expense is to be recognized, the intrinsic value approach in APB Opinion 25 not only fails to completely reflect the potential influence of share options on diluted earnings per share, but also affects accurate profitability assessment. The FASB had noticed that there were several deficiencies in APB Opinion 25 and had been working on a project to contemplate various methods of estimating share-based compensation costs since 1984. At the same time, in the early 1990s, the US Congress was also involved in setting the accounting rules for employee share options, especially after its (and the press') awareness of the fact that executives of large US companies were much more highly paid than their counterparts in other countries, and share options usually made up a dominant proportion of their remuneration. Questions were brought forward about whether the then accounting rules could enable shareholders to exactly discover how much their companies' executives were being paid and whether the executives' pay was in line with their performance. A hearing, the general content of which could be seen from its title 'Stealth Compensation of Corporate Executives: Federal Treatment of Stock Options', was held in January 1992; during the hearing, the SEC and the FASB were forced to accelerate their efforts to formulate accounting rules which were capable of 'accurately reflecting the value of [stock] options to the people receiving them and the cost of these options to the companies that issue them (extracted from the Senator who chaired that hearing)'. In such a backdrop, the FASB issued an exposure draft *Accounting for Stock-based Compensation* (the FASB 1993 Stock Options Exposure Draft) in June 1993, which would have required companies issuing share options to employees to estimate the fair value of the options and record a corresponding expense in their income statements.

From the perspective of accounting, APB Opinion 25 prescribes that the intrinsic value of a share option is measured at grant date only, nonetheless, during the vesting period, namely, the period between the option grant date and the date when the option holder can actually exercise it, the market price of the underlying share may change, and then the option holder is able to realize the option's intrinsic value at the date of exercise because of having held the option, that is to say, the option holder can make future gains from increases in the share price; moreover, the option holder does not pay the exercise price until the exercise date. Consequently, besides the intrinsic value, which is identical to that identified under APB Opinion 25, the fair value of share options embraces two other elements: the time value of money and the time value associated with volatility; that makes fair value always greater than intrinsic value. Conceivably, the fair value approach provides a measure of the share option's total value, which is capable of more faithfully representing share-based payment transactions between the entity and its employees. The transaction, whereby the entity grants share options to employees for their services, occurs on grant date, so the grant date is regarded as appropriate to both recognition and measurement. As employee share options cannot be sold on the market, in other words, no market prices are available, additionally, making a reliable estimate of the value of employee services received is typically impracticable (logically, the former is a surrogate measure of the later), consequently, it is needed on grant date to evaluate the quantification of the fair value of share options and the allocation of expense over future periods. In this case, there could be some practical difficulties with estimating, for instance, allowing for the fact that not all options initially granted will ultimately vest, and using valuation technique, usually an option pricing model which is based on assumptions such as expected volatility and expected dividends, to approximately calculate the fair value of the option. On the whole, even if the requirement for recognition of compensation cost for the granting of share options is theoretically sustainable, controversies would be existing in fair value reporting of options, or to say it another way, valuation techniques for financial instruments, including employee share options, are still continuing to evolve (the discussion on fair value being taken as measurement attribute can be referred to paragraphs B51-B68 of SFAS 123; paragraphs BC61-BC105 of IFRS 2). In history, the FASB 1993 Stock Options Exposure Draft met with vehement opposition from the preparer community, but that was not caused by the accounting reasons above mentioned.

Noticeably, the executives who received huge quantities of share options would never let their interests be threatened, and they were unconcerned with such specific accounting issues as the application of certain valuation model, but resolutely not tolerant of the proposal that employee share options should show up as a charge against a company's earnings, in all likelihood it was because they thought this change could threaten their share options. It could be imaginable that those high-ranking executives would not resort to the FASB, but directly to the Senate and the President. Some main events relating lobbying on employee share options were as follows: From October 1993, several Congressional hearings were held, most of the witnesses invited to testify were representatives of companies and trade associations, they and six members of Congress on behalf of Silicon Valley were all opposed to the FASB's proposal, few FASB supporters were invited to explain the FASB's reasoning. As far as the detailed arguments are concerned, those executives definitely could not say that the main reason for their opposition was because they would be personally harmed, instead, because that the new accounting rule in the FASB 1993 Stock Options Exposure Draft would destroy the high-tech industry, damage the US corporate economy, lead to depression, and even end capitalism. What merits attention is that those reasons did not sound pretty dissimilar from the ones mentioned in the above instance of business combination, and surely could not justify why an improved accounting rule was capable of bring the US to collapse. Moreover, in March 1994, an anti-FASB gathering, which was named as Silicon Valley Employee Stock Option Rally, was held. That rally carried strongly propagandizing implications, as evidenced by exaggerated posters, emotional speeches, media coverage, and so on, a petition against the FASB's position was signed for transmission to the President, and on the same day as the rally was held, the FASB was convening nearby the West Coast public hearing. Shortly after the FASB's public hearings, the Senate began to take its actions. In May 1994, although most of Senators had little information about share options, in the agitation of some very powerful Senators, the Senate passed a sense-of-the-Senate resolution, in which the key passages are that the FASB should not proceed with the new accounting treatment of employee share options, because that would 'have grave economic consequences particularly for business in new-growth sectors which rely heavily on employee entrepreneurship'. Obviously, it is political power, and yet very strong political power that intruded into accounting standard setting. Pressure from the Senate continued after the passage of that resolution. In October 1994, a very hard and highly influential Senator, who was the main sponsor of the above-mentioned resolution, introduced the Accounting Standards Reform Act of 1994, which would have required the SEC to pass on all new accounting standards, specifically, that bill stated that 'any new accounting standard or principle, and any modification… shall become effective only following an affirmative vote of a majority of a quorum of the members of the [Securities and Exchange] Commission'. It is evident that the bill was targeted at share compensation project, but it went well beyond the issue of accounting for employee share options, thereby directly threatening the survival of the FASB. If that bill had been enacted, interest groups could have gained direct control of the process of setting accounting standards by holding sway over the SEC, hence making the FASB, as a private independent body, redundant. (That bill had not been adopted, because the FASB dropped the share option proposal.) In summary, the above description shows that the strength of the lobbying campaign for accounting for employee share options was unprecedented, not least the political pressure from the key powerful Senators made the FASB unable to keep acting on the subject of share options, and even put the existence of the FASB in question. Finally in October 1995, regardless of its assertion that recognition of compensation expense based on the fair value of options issued to employees is conceptually correct, the FASB could do no more than issue SFAS 123 *Accounting for Stock-Based Compensation*, in which it expressed a preference for the fair-value-based method, but still permitted continued application of APB Opinion 25's intrinsic value method, at the same time, required footnote disclosure of the impact on earnings as if the fair value approach had been used. Although it is generally accepted that inadequate recognition and/or measurement could not be recompensed for fully by expanded disclosures, supplemental disclosure is better than nothing; some of enterprises remained averse to even the footnote disclosure requirement, but Congress did not intervene this time (the discussion about how SFAS 123 was framed could be referred to Zeff, 1997; Rosenfield, 2006: 383-398).

From the case of accounting for share options, it is visible that in the process of formulating SFAS 123, under strong political pressure, the FASB's conceptual frameworks could not have any chance of being used at all; nor could the principle of serving users' information needs (which was shown in the conceptual framework SFAC 1 as the objective of financial reporting, mentioned on page 61) be used to guide accounting standards setting; and nor could the principle of representational faithfulness (which was included in SFAC 2 as a qualitative characteristic, mentioned on page 65) be utilized to expatiate upon why the fair value approach could faithfully represent the economic transactions that the entity receives and consumes employee services in exchange for share options. Zeff (1978) points out that '[the FASB is faced with] a dilemma which requires a delicate balancing of accounting and nonaccounting variables. Although its decisions should rest - and be seen to rest - chiefly on accounting considerations, it must also study - and be seen to study - the possible adverse economic and social consequences of its proposed actions'. 'What is abundantly clear is that we have entered an era in which economic and social consequences may no longer be ignored as a substantive issue in the setting of accounting standards. The profession must respond to the changing tenor of the times while continuing to perform its essential role in the areas in which it possesses undoubted expertise'. In an article titled ''Political' Lobbying on Proposed Standards: A Challenge to the IASB', Zeff (2002) illustrates another point that 'political' represents self-interested considerations or pleadings by preparers and others that may be detrimental to the interests of investors and other users, a phenomenon that has been associated with the term ‘economic consequences’. Through the four cases above cited in this section, it could be revealed that in the process of setting accounting standards, the FASB might hope that conceptual frameworks could be used to offset a certain amount of influence form political lobbying, but as a private body, it had no power to enable conceptual frameworks to perform a (dominant) function. Whether or not a standard can be created has no necessary connection with whether or not a conceptual framework has existed, because the process of setting standards, just as pointed out by Zeff (1978), can be affected not only by accounting related factors, but also by nonaccounting related ones; even if the accounting logic of a standard is simple and sensible, the process of framing that standard could be complicated and full of controversies, which do not relate to accounting in most circumstances. The below contents are some relative additions to the above example of employees’ share options: In February 2004, the IASB issued IFRS 2 *Share-based Payment*, which only allows the fair value approach, specifically, IFRS 2 requires that an entity should recognize an expense for employee services received in share-based payment transactions at the fair value of employee share options (since the value of employee services cannot be determined), and the fair value should be estimated by using an option pricing model (the standard does not specify which particular model should be used) at grant date. To a considerable degree, owing to the influence from IFRS 2, but more importantly, because of the fact that political lobbying against expensing the options at fair value became somewhat faltering in the wake of scandals surrounding Enron and others, in December 2004, the FASB made revisions to SFAS 123 and changed its title into ‘Share-Based Payment’. The newly revised SFAS 123 eliminated the intrinsic value method, and this time around, Congress and the government did not hinder the issuing of the new standard. As for Chinese GAAP, the relative standard is ASBE 11, the title of which is identical with SFAS 123 and IFRS 2. Compared with IFRS 2, ASBE 11 only covers share-based payment transactions for services provided by employees and other parties, does not address transactions in which the entity receives goods and the payment type of equity settled with cash alternatives (because such occurrences are quite rare in China), the detailed accounting treatments in ASBE 11 are similar to IFRS 2. Furthermore, from January 1991 onwards, all FASB standards must be approved by at least a two-third majority, that is to say, the minimum number of affirmative votes has to be five when seven members are voting, prior to this, passage of a new standard just needed a simple majority. For example, the controversial SFAS 87 above mentioned, which was issued in 1985, was passed only by a vote of 4-3, and SFAS 123, which was published in 1995, by 5 assenting and 2 dissenting votes, both of which were approved by the lowest votes required; the revised SFAS 123 announced in 2004 was adopted by an unanimous vote. The reason for mentioning this topic is because an extent to which the disagreements are involved in certain accounting standard and some causes probably concerning either accounting or nonaccounting, which result in these contentions, might be perceived from it.

3. IASB in the EU

The reason why the instances of the US accounting are given to elucidate the role of conceptual frameworks in accounting standards setting is because that there is no tangible background of political power, and political influence on the framing of IASB GAAP is not so obvious, but the process of adopting IASB GAAP could still be political. The following is a brief description of the application of IFRSs in the European Union (abbreviated to the EU, note: henceforward reference to the EU includes the former European Economic Community and the European Community): Since the founding of the EU in 1957, one of its fundamental objectives has been the creation and maintenance of a common market among its members, including the freedom of establishment for firms and the free movement of capital, this, to a substantial extent, entails harmonizing the financial disclosure of companies in the EU. At the prior stage of voluntary adoption of internationally recognized rules, most of large European companies tended to adopt US GAAP, which the EU had no say on. In 1995, the EU became an observer on the then IASC Board, and was exerting increasingly significant effects upon the IASC's (later, the IASB's) activities. In 2002, the EU formally enacted the so-called IAS Regulation (note: the EU attempts to fulfil the harmonization of financial reporting through legislation, including two main instruments: directives and regulations; and, in contrast to a directive, which requires legislation by member states, a regulation takes effect throughout the EU without having to be transformed into national law), which stipulates a compulsory application of the IASB's standards (certainly, and interpretations) for the consolidated statements of European listed corporations from 2005 onwards. What deserves attention is that IASB GAAP was not directly used per se to prepare European listed consolidated accounts, if that had been the reverse, the EU, in substance, would have delegated the development of accounting standards to an international small private sector body over which the EU has no control. In order to avoid such a political problem as losing power of setting standards, the IAS Regulation set up an elaborate organization, known as the endorsement mechanism, to tackle its relation with the IASB and to decide whether or not to adopt an IASB standard. Specifically, for the sake of assisting the European Commission, which consists of politicians nominated by the EU member states and is the EU's supreme executive branch, in determining whether or not to endorse an IASB standard, two new committees were established in 2001. The one is the European Financial Reporting Advisory Group (EFRAG), a private sector committee of preparers, auditors, and the like, the principal functions of which are to provide a technical assessment of IFRSs in the European context and to contribute to the work of the IASB on a proactive basis, for example, by commenting on exposure drafts. The other one is the Accounting Regulatory Committee (ARC), which is composed of government representatives from the EU member states and chaired by a representative of the European Commission, and is a body with political properties. The main function of the ARC is to make decision on whether or not to endorse an IASB standard (in practice, the process is whether or not the ARC consents to the European Commission's proposal to adopt or reject an IFRS) after taking account of the technical recommendation report presented by the EFRAG and other political aspects, for instance, whether a certain standard is in accordance with the EU law, or whether the government of a member state is bitterly opposed to the standard. If the ARC disagrees on the endorsement of a standard, the European Commission still can ask the Council of Ministers (note: its official name is the Council of the European Union, which is formed through each member state choosing a minister and is one of the two chambers of the EU's legislative branch, the other chamber being the European Parliament) to override the ARC's decision. In addition, the final endorsement of IFRSs requires either approval from the European Parliament and the Council of Ministers or no opposition from them within three months. It is evidently revealed that the whole process of the endorsement really is lengthy and bureaucratic, and the EU's endorsement mechanism, which is founded by political power and possesses intense political property, can inevitably expose the process of setting the IASB's standards to political pressures.

A representative instance of how the IASB has been affected by politics could be the endorsement of IAS 39. IAS 39 is a standard first published in 1999, and the topic involved in it is primarily about the valuation of financial instruments. This is a very complex and contentious subject, to a considerable extent, because cost or amortized cost is not an appropriate form of measurement for most of financial instruments, to take an example, the historical cost of a futures contract is nearly zero, but that contract is very likely to bring its holder an enormous amount of assets or liabilities. The original IAS 39 is perceived to be imperfect, chiefly because it is excessively rules-based, embodies a good number of options, and moreover it is inconsistent, requiring certain financial instruments to be measured at fair value and others at historical cost. In 2002, the IASB issued an exposure draft that proposed amendments to IAS 39, and subsequent to that, the IASB received plenty of critical comments from the financial community. The objections from a lot of banks and insurance companies, not least from Continental European ones, were mainly to the use of fair value accounting for financial instruments and hedging provisions. To put it simply, the Continental European banks, first of all, were opposed to the prohibition against their continuation in valuing many financial instruments according to how much they paid for them, their major reason for doing so was that measuring the financial instruments at fair value at balance sheet date would result in increasing profit or loss volatility. The IASB's debate on volatility is that balance sheets should reflect the volatility feature of the marketplace, but should not pretend that there is stability when there is not (note: this point was mentioned on page 77 as well). And then, the banks were also averse to restrictions on the requirements that must be met so as to apply hedge accounting. To briefly make an introduction to the relative background, hedge accounting is a way of presenting gains or losses on hedging instruments, typically derivatives, in a manner that is in an attempt to minimize the impact of profit or loss volatility; as hedge accounting constitutes a beneficial presentation, only under some circumstances, which are probably quite complex (even supposing that the general principle of achieving hedge accounting, i.e. the instrument should be highly effective in hedging a particular exposure, is straightforward), entities can apply it (as to the discussion about IAS 39, see Walton, 2004; Spooner, 2007: 370-384). According to the comments it received, the IASB made some revisions to its exposure draft, but could not fully gratify the requests of the banks on the Continent. Following their failure to make the IASB completely satisfy their requests, those banks which were accustomed to income smoothing began lobbying through the EU's endorsement mechanism, for example, they appealed to the French president of the day and successfully persuaded him into intervening. (At this point, there is a further cause, which is that French rules on accounting are formulated by the public authorities and institutions attached to authorities, and preparers greatly affect the creation of accounting standards. Needless to say, the topic of French accounting is outside the scope of the thesis.) In July 2003, the French president wrote to the President of the European Commission, saying that the exposure draft would make bank's figures volatile and destabilize the European economy, so it should not be approved. Presumably, there is no substance in the letter by the President of France, as it is impossible to envisage that the economic stability of a country could be grounded on accounting income smoothing. This is a noticeable case that political power interferes in the technical contents of an accounting standard (see Alexander, 2006). In view of the fact that Continental European banks and the French government were fiercely opposed to the accounting treatment of financial instruments prescribed by IAS 39, in 2004, the EU endorsed IAS 39 with two so-called carve-outs: one was that the (optional) fair value measurement of liabilities is not permitted, the other one was to broaden the applicability of hedge accounting to core deposits. The partial endorsement from the EU posed a threat to the whole standard setting process of the IASB, the IASB had to make alterations to accounting standard in compliance with the EU's requirements. From 2002 onwards, the IASB published some exposure drafts and made revisions to IAS 39 many times; the current situation is that IAS 39 is fully endorsed in effect. Since 2008, the IASB has commenced with a large project to improve and simplify the classification and measurement requirements for financial instruments, the objective of the project possibly expect all financial assets and liabilities to be measured at fair value on the balance sheet. To revert to conceptual framework, the IASB Framework is not included in IASB GAAP, the EU did not endorse it either, consequently, it was not referred to in the debate on IAS 39, and furthermore, accounting principles could never be practically useful in such kind of argument full of politics. (Provided being considered from the angle of the IASB Framework, gains and losses that result from changes in their fair values cannot be deferred on the balance sheet, since such gains and losses are not in compliance with the definitions of assets and liabilities; see Hague (2004) for a detailed analysis of the principles underlying IAS 39.) From this instance of the adoption of IAS 39, it can be manifested that the creation of the endorsement mechanism is not truly aimed at rejecting an IFRS, in that case, the set of IFRSs applied in the EU would be different from the rest of the world, that would not be ideal for capital markets. The intention of endorsement mechanism is presumably to let the IASB experience the threat from the rejection of a standard, therefore, the EU (through the EFRAG) could become influential in the development of final standards; as to the IASB, if its standards can only be partly endorsed, the EU will possibly abandon IASB GAAP (the subject about accounting in the EU discussed in this and the last paragraphs could be read in Flower, 2004b: 159-166, 189-191; Benston et al., 2006: 149-153; Alexander and Archer, 2007: 1.10-1.12). Incidentally, it is hard to imagine the Chinese government would be able to give up its power over accounting standards setting, the application of IASB GAAP in China could be a prolonged and intricate political process; more discussion about this issue will be detailed later. Now that conceptual frameworks, owing to powerful political sway over which, have been unable to adequately function amid accounting standards setting (and adoption), why do standard setters still keep developing conceptual frameworks? The previous section of this chapter once mentioned differentiation between accounting standards and accounting standards setting (see page 123), even if the process of setting accounting standard is not guided by conceptual framework, the framework can be used to explain or underpin an accounting standard all the same, and the following are two more cases about this point.

4. contingencies and joint ventures

The first instance is about contingencies, which in IASB GAAP are included in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. In respect of contingent liability, IAS 37 assigns two meanings to it: (a) a possible present obligation whose existence can be confirmed only by the occurrence or nonoccurrence of one or more uncertain events not entirely within the entity's control and (b) a present obligation that is not recognized either because an outflow of resources to settle it is not probable, or its amount cannot be measured reliably (see paragraph 10 of IAS 37). IAS 37 stipulates that an entity should not allow formal recognition to a contingent liability, instead, the entity should disclose information on the contingent liability in the notes; additionally, the requirements for disclosure may be unnecessary if the possibility of any outflow of economic resources in settlement is remote (ibid, paragraphs 27 and 86). In addition to contingent liabilities, IAS 37 presents a detailed guidance on the topic of provisions, interpreting a provision as a present liability with uncertain timing or amount of future cash flows, and provides that a provision should be recognized in the balance sheet (plus the stipulated disclosures in the notes) if it is probable that an outflow of resources will be required to settle the liability and a reliable estimate of the amount of the liability can be made (ibid, paragraph 14). Amid the foregoing, IAS 37 elucidates 'probable' above mentioned as 'more likely than not' to occur, or to put it simply, a 51 percent of probability of the existence of a present obligation from past event will create a provision on the balance sheet (given that the recognition criteria are met at the same time), while a 49 percent of probability in such circumstances will produce a contingent liability, which will not qualify for recognition on the balance sheet (see the decision tree shown in Appendix B of IAS 37). The pertinent standard in Chinese GAAP concerning this issue is ASBE 13, and its specific requirements are the same as IAS 37. In June 2005, as part of the convergence project with the FASB, the IASB issued an *Exposure Draft of Proposed Amendments to IAS 37 and IAS 19* (henceforth called as the 2005 Liabilities Exposure Draft), which made complicated and radical changes to the present practice. To put it briefly, that proposal holds that many items previously described as contingent liabilities satisfy the definition of a liability in the IASB Framework, on the grounds that the contingency is relative to uncertainty about the amount that will be required to settle a liability rather than uncertainty about whether a liability exists, and then that exposure draft advocates the elimination of the term 'contingent liability' (paragraphs BC23-BC29 of the 2005 Liabilities Exposure Draft). En passant, the IASB Framework defines a liability as 'a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits' (paragraph 49 (b) of the IASB Framework). Moreover, the IASB proposes replacing the term 'provision' with 'non-financial liability', and prescribes that an entity should 'recognize a non-financial liability when: (a) the definition of a liability has been satisfied, and (b) the non-financial liability can be measured reliably' (paragraph 11 of the 2005 Liabilities Exposure Draft; visibly, the IASB emphasizes that recognition and measurement considerations should not be used to determine whether a liability exists or not); it is noticeable that, compared with the existing requirements, this alteration might make more liabilities be presented on the balance sheet. Correspondingly along with the elimination of provisions and contingent liabilities, the 2005 Liabilities Exposure Draft proposes omitting the probability recognition criterion in paragraph 14 of IAS 37 above indicated, because the uncertainty of the amount and timing of the outflow of resources cannot represent whether there is the uncertainty of the outflow or not. The IASB stresses that applying the probable outflow criterion to the conditional obligation (another one is unconditional obligation) is contradictory to the IASB Framework, owing to the fact that paragraph 82 of the IASB Framework describes recognition as 'the process of incorporating in the balance sheet or income statement an item that meets the definition of an element', or to say, the probability recognition criterion cannot be used to decide on whether a liability exists or not (ibid, paragraphs BC36-BC48). In January 2010, the IASB published *Measurement of Liabilities in IAS 37* (afterwards called as the 2010 Liabilities Exposure Draft) to re-expose the IAS 37 measurement requirements. The 2010 Liabilities Exposure Draft deems it ambiguous and arbitrary that paragraph 36 of IAS 37 demands entities to measure the liabilities at 'the best estimate of the expenditure required to settle the present obligation at the end of the reporting period', and then proposes to delete the term 'best estimate', further suggests that the measurement should be the amount that the entity would rationally pay at the measurement date to be relieved of the liability. This kind of way to estimate a liability involves taking account of the expected outflow of resources, that is, the probability-weighted average of the outflows for the range of possible outcomes (but not just the most likely outcome required by the current standard), the time value of money and the risk that the actual outflows might ultimately differ from the expected outflows. The IASB believes that the advantage of this method is to capture value-maximizing behaviour and to be unnecessary to take costs, which could be arbitrary, as the basis of measuring (paragraphs 36, BC2-BC4, BC9-BC 22 of the 2010 Liabilities Exposure Draft). However, under this method, a hypothetical profit margin is embraced in the measurement of the liability, and that may provide earnings management with a means (ibid, paragraphs AV2-AV4). It is observable from this example that the amendments to IAS 37 by the IASB, to a large extent, are grounded on the consideration of conceptual framework, and that could be illustrated by the requirement of identifying a liability through its definition in the IASB Framework.

Similarly, the second instance is about the joint ventures project. The current IASB GAAP relative to accounting for investments in joint ventures are contained in IAS 31 *Interests in Joint Ventures*, paragraph 3 of the standard provides the following definitions: 'A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control'. 'Joint control is the contractually agreed sharing of control over an economic activity, and exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control (the venturers)' (note: do not confuse this with common control mentioned on page 7). Joint ventures can take many different forms and structures; that basically (but neither exclusively, nor always decisively) depends on the dissimilarities of the legal forms of arrangements, IAS 31 identifies three different types, referred to as jointly controlled operations, jointly controlled assets, and jointly controlled entities (paragraph 7 of IAS 31). Of which the main type of joint ventures is the jointly controlled entity, which usually is a partnership and registered as an independent legal entity, in which each venturer has an interest and a form of joint control over the economic activity of the entity. A jointly controlled entity controls the assets of the joint venture, incurs liabilities and expenses, and earns income on its behalf; and maintains its own accounting records and produces its own financial statements as well. Normally, each venturer would share the results of the jointly controlled entity in proportion to its ownership interest (paragraphs 24-29 of IAS 31). As for accounting treatments for interests in jointly controlled entities, IAS 31 allows a venturer to make its choice between proportionate consolidation and the equity method with a main aim of reflecting the economic substance and reality, rather than surface and form, of the contractual arrangement (ibid, paragraph 30). The benchmark treatment is the use of proportionate consolidation, which requires a venturer to combine its proportionate share of all assets, liabilities, revenues, and expenses of the jointly controlled entity with similar items in the venturer's financial statements on a line by line basis (ibid, paragraphs 3 and 33). As an alternative, a venturer should use the equity method to report its interest in a jointly controlled entity (ibid, paragraph 38). To put it simply, under the equity method (there is a detailed description in IAS 28 *Investments in Associates*), 'an interest in a jointly controlled entity is initially recorded at cost and adjusted thereafter for the post-acquisition change in the venturer's share of net assets of the jointly controlled entity, [and the] profit or loss of the venturer includes the venturer's share of the profit or loss of the jointly controlled entity' (paragraph 3 of IAS 31), in other words, only a single line in the venturer's balance sheet is presented for reflecting the venturer's net investment in the jointly controlled entity, identically, the venturer's share of the jointly controlled entity's net income or loss is shown as a single line item on the venturer's income statement. The different methods of accounting could create a massive impact on the financial statements of the venturer, that could be manifested by the fact that only the amounts of profit for the period and total equity still remain unchanged under different methods. (Incidentally, to mention the below things: when a venturer has no longer had its joint control over a jointly controlled entity, the proportionate consolidation method should be discontinued; or when a venturer has not retained joint control or significant influence over a jointly controlled entity, the use of the equity method should be discontinued; in the couple of cases, the provisions relative to investments in IAS 39 should be applied. When a jointly controlled entity becomes a subsidiary of a venturer, the venturer should account for its interest in accordance with IAS 27 *Consolidated and Separate Financial Statements*. From the date on which a jointly controlled entity becomes an associate of a venturer, the venturer should account for its interest in conformity with IAS 28. The specific requirements are referred to the relative standards, from these multiple types of business relationships and various methods of accounting, it could be noted that accounting for fixed asset investments possibly lacks an appropriate principle in this respect. In addition, whether or not the equity method of accounting for investments can be used is dependent upon the condition that the investor is able to exercise significant influence (paragraph 2 of IAS 28 defines significant influence as 'the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies') over the investee (such an investee is known as an 'associate' in IASB GAAP), paragraph 6 of IAS 28 prescribes that '[i]f an investor holds, directly or indirectly, 20 per cent or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case'. It is not difficult to find that the threshold of 20 percent of voting shares is representative of arbitrary and numerical accounting rules, moreover, significant influence is not a principle which could be read in the IASB Framework (Nobes, 2005).) As regards the stipulations in Chinese GAAP, the corresponding standard is ASBE 2 *Long-term Equity Investments*, which does not involve the accounting treatments for jointly controlled operations and jointly controlled assets, and only allows a venturer (the investing enterprise) to use the equity method to recognize its interests in a jointly controlled entity (the investee enterprise), the joint ventures in China will be discussed in chapter 7 again.

Compared with IASB GAAP, US GAAP, under most circumstances, only allows corporate joint venturers (analogous to jointly controlled entities in IAS 31 terminology) to be accounted for by the equity method (some exceptions permit proportionate consolidation, see APB Opinion 18 *The Equity Method of Accounting for Investments in Common Stock* and other relative requirements). As a part of a project converging with US GAAP, in September 2007, the IASB issued an exposure draft ED 9 *Joint Arrangements* (afterwards it is called as the 2007 Joint Ventures Exposure Draft). The exposure draft first points out the problems with IAS 31, for instance, IAS 31 allows an option of using either the equity method or proportionate consolidation, and such an option could lead to similar transactions being accounted for in different ways and, therefore, impair comparability, which is a principal qualitative characteristic in the IASB Framework (paragraphs 39-42 of the IASB Framework). The 2007 Joint Ventures Exposure Draft deems that proportionate consolidation is not an appropriate method of accounting for jointly controlled entities, on the grounds that the proportionate share of assets and liabilities of the jointly controlled entity recognized on a venturer's balance sheet is not in accordance with the definitions of an asset and a liability in the IASB Framework (the two definitions are on page 37 and page 106 respectively), as every venturer simply has control over its investment in the jointly controlled entity, but does not assume any control on or obligation to items of the jointly controlled entity (paragraphs BC5-BC14 of the 2007 Joint Ventures Exposure Draft). As for how to make improvement, the IASB proposes replacing the term 'joint venture' in IAS 31 with 'joint arrangement', and classifying joint arrangements into two types: joint operations (similar to jointly controlled operations and jointly controlled assets in IAS 31), and joint ventures (equivalent to the jointly controlled entities in IAS 31); and suggests that proportionate consolidation be eliminate, and a venturer should recognize its interest in a joint venture using the equity method (paragraph 23 of the 2007 Joint Ventures Exposure Draft). The suggestion put forward by the IASB could not be uncontroversial, just as mentioned in paragraph 40 of the existing IAS 31, proportionate consolidation is likely to be viewed as being able to better present the true scope of an entity's operations. It is not difficult to notice that in the reasons explained by the IASB for the amendments to IAS 31, whether or not a certain specific accounting method is in accordance with the IASB Framework is one of the important factors for consideration. The above two instances of the review on and improvement to the current standards by the IASB could make it perceptible that accounting principles set out in a conceptual framework could be used to describe and uphold an accounting treatment or method.

To make a brief summary:

By now, the foregoing in this chapter has made use of the instances of the US and international accounting to discuss the relationship between conceptual frameworks, accounting standards, and accounting standards setting, and this point is once mentioned at the beginning of chapter 4 (see page 59). This thesis suggests that a distinction could be drawn between accounting standards and accounting standards setting. As for the relationship between conceptual frameworks and accounting standards, to take IASB GAAP as an example, it could conceivably be believed that the standards in the current IASB GAAP relating to construction contracts (IAS 11), deferred tax (IAS 12), leases (IAS 17), employee benefits (IAS 19), and so on, may not be satisfactorily explained by the IASB Framework. However, the relation between IFRSs and the IASB Framework could be observed from the below two aspects as well: First, from an complete perspective, there are a great deal of descriptions on the connection between accounting standards and the IASB Framework in IASB GAAP, even if plenty of them are debatable, for example, in IAS 12 (about the use of the balance sheet liability method to account for deferred tax and not allowing the discounting of deferred tax assets and liabilities, on pages 85 and 86), in IAS 20 (on the application of the deferred income approach in recording government grants related to assets, on pages 90 and 91), in IAS 17 (on the application of substance over form to lease accounting, on page 94), in IAS 19 (about allowing to make use of the 'corridor' approach to present actuarial gains and losses, on page 109), and so forth. Second, from a developmental perspective, in spite of the controversy over the proposals, the improvement projects of the IASB, for example, the revenue recognition project (above mentioned on pages 78 and 79), leases project (on page 98), liabilities project (on pages 142 and 143), and joint ventures project (on pages 147 and 148), all take a sizeable consideration of the IASB Framework. From the two perspectives above discussed, namely the complete one and developmental one, the IASB indeed uses the IASB Framework to explain and uphold IFRSs, and this action itself manifests that there is the concept of considering conceptual framework in IASB GAAP, regardless of whether or not those explanations and arguments are uncontroversial, or controversial, or highly controversial. The reason why conceptual frameworks cannot perfectly explain accounting standards could be, to a great extent, that accounting, naturally including conceptual frameworks, has its inherent limitations; in the words once mentioned above, the core essence of accounting, namely the accounting's X, has not been grasped, nor even known by human beings, hence any explanation may just be an approximation of that X (the opinion about the approximation of the accounting's X is also mentioned on page 125). As far as the relationship between conceptual frameworks and accounting standards setting is concerned, from the above mentioned process of the formulation of SFASs 141 and 142 (on pages

117-119), SFAS 69 (on pages 126-128, certainly, that is prior to the issue of conceptual frameworks), and SFAS 123 (on pages 131-134), the process of the application of IAS 39 in the EU (on pages 138-140), and other examples, it is manifested that conceptual frameworks do not play a role in accounting standards setting (and adoption). The reason for that is mainly because the accounting standard setting body of private sector such as the FASB and the IASB has no power, their power is ultimately derived from political power, and a certain accounting policy could have economic consequences for a business, therefore, management could lobby the authorities to exert political pressure, and then the process of setting and adoption of accounting standards is politicized, conceptual frameworks developed by standard setters without power could hardly serve any function in the process full of political influence (see Solomons, 1978; Zeff, 1978). Solomons (1989, reprinted in 1997) writes out 'Guidelines for Financial Reporting Standards', and deems that applying accounting principles, for example the asset and liability view (mentioned on pages 41 and 42 of this thesis), into setting standards could make accounting standards more consistent and logical, those seems rational considering conceptual frameworks could explain and uphold accounting standards; while Macve (1981, 1983a, reprinted in 1997) holds that conceptual frameworks cannot provide explicit guidance on practical problems, hence no need for them, and points out that the aim of creating conceptual frameworks is to enable standard setters to retain the right to formulate standards, those sounds reasonable considering that conceptual frameworks cannot function in the politicized process of accounting standards setting.

As was stated above, the IASB and the FASB in 2004 commenced a joint project to develop an improved, common conceptual framework, the project's overall objective is to create a sound foundation for future accounting standards that are principles-based, internally consistent and internationally converged. The first phase of the project was completed in 2010, which deals with the objectives and qualitative characteristics of financial reporting; afterwards, the project was paused. AAA's FASC (2010, this paper does not mention the suspension of the project) attempt to address issues with the current conceptual frameworks. The critique on the existing conceptual frameworks and the project in progress holds that such things as 'objectives', 'qualitative characteristics' and so on in a conceptual framework are too lofty criteria for the making of accounting standards. These general statements are impossible to be disagreed with, it is for this reason, they cannot become the specific principles which will guide the formulation of future accounting standards, in another words, people are unable derive practical accounting implications from, for instance the 'objectives'. Subsequently, that paper puts forward its suggestions for what a conceptual framework should be, mainly including five principles: recognition and measurement rest on interpreting transactions, operating activities separate from financial activities, the centrality of operating earnings measurement, balance sheet conservatism, and owner's equity accounting rests on a proprietorship perspective, and the financial statements based on the above five proposed principles. Certainly, the conceptual framework raised by the paper is fundamentally different from the current conceptual frameworks; in 2012, the IASB decided to restart the project, chiefly focusing on elements, measurement, presentation, disclosure and reporting entity, so it could be seen that the IASB is not intending to adopt the suggested model proposed by AAA's FASC (2010), at least at present.

Reverting to the issue of Chinese accounting, at the beginning of chapter 4 (see page 60), it is mentioned that this chapter tries to study what the role of the 2006 Basic Standard in Chinese GAAP is, as stated above, the process of accounting standards setting is heavily politicized, conceptual frameworks are unable to play a role in it (that point is the main argument of the above writing), and now that Chinese accounting standards have been formulated by the government, why does Chinese accounting standard setter still keep developing conceptual frameworks? Peasnell (1982) argues that the importance of a conceptual framework is related to the power and responsibilities of standard setters. To demonstrate this, he identifies three alternative institutional arrangements: more or less complete laissez-faire, state control and supervision, and delegation of power to the profession; in addition, there are further three forms in the last arrangement: (1) the regulatory body delegates the responsibility to the accounting profession while retaining power (for example, the situation in the US), (2) the power is in the hands of the accounting profession with the responsibility controlled by a government agency, and (3) both power and responsibility reside in the profession. Peasnell concludes that only when both the power and responsibility are in the hands of an accounting professional body, does a conceptual framework play an obvious role; a conceptual framework is of little use in any other types of institutional arrangement. Having analyzed the elucidation by Peasnell (1982), Xiao and Pan (1997, note: the discussion in that article is about the 1992 Basic Standard) point out that the situation in China does not support Peasnell's conclusion, they hold that 'the presence and the central role of the [MOF] have enhanced the role of [the 1992 Basic Standard] in the Chinese case. The problem of the old approach to accounting regulations adopted by the [MOF] is one of the main reasons that the ministry opted for a [conceptual framework]. Its use of a [conceptual framework] was also attributable to the fact that the ministry had had no experience in setting standards in a market economy and to the fact that the standard-setting program has been a means of implementing the country's open policy and, thus, a [conceptual framework] would enhance the creditability of its accounting standards'. The topic of the role of conceptual frameworks could also be observed from the below angle: Prior to the question about the role of the 2006 Basic Standard in Chinese GAAP, it could be asked first whether it is true there is a conceptual framework in Chinese GAAP. The answer is that there is indeed a 11-page and 50-Article conceptual framework in Chinese GAAP (i.e. the 2006 Basic Standard, the terms of which is similar to the IASB Framework terms, but it merely enumerate those terms instead of offering any further explanation about them), but section 3 of chapter 4 mentions many times that Specific Standards never give any indication of how they are based on the 2006 Basic Standard, for instance, on page 86 (about ASBE 18), on page 89 (about ASBEs 18 and 1), on page 91 (about ASBE 16), on page 94 (about ASBE 21), on page 106 (about ASBEs 27 and 19), and so on. Therefore, it could be deemed that Chinese accounting does not possess the concept of considering conceptual framework (or to say, no conceptual frameworkism, which could be abbreviated to [no] CFism), even if it possesses a conceptual framework.

5. tentative conclusion and further differences identified

This chapter explicates the primary contents and functions of Chinese and international conceptual frameworks by exemplifications with one aim of answering the research question of this thesis, in addition, another aim is, by illustrating those instances, attempting to demonstrate what are principally and basically incorporated in accounting, as an independent academic discipline (if possible). At this place, one respect needing stress is that accounting, in virtue of its attribution as a social science, could decide the fact that the conclusion drawn by the later generation in their research into accounting is not certain to surpass the one by the former generation. To take an example, Bromwich (1985: 72-107) analyses, in the context of the UK, the institutional framework for accounting standard setting and the respective advantages and disadvantages in (the presumed) legislative accounting regulation and self-regulation by the accounting profession, and argues (ibid: 113 and 114) that, from the angle of economics, accounting standard setting could be looked on as a redistributive exercise (or to say, the new accounting policies may cause resource re-allocation), as a result, in a practically non-existent circumstance that ideally functioning markets exist and have obtained equilibrium, any accounting regulation may aid some sections of society at the expense of others, subsequently the attainment of a set of accounting principles (that is a conceptual framework) which are useful to all irrespective of their preferences may be regarded as impossible in the present state of knowledge. Archer (1992; 1993), in terms of philosophy, surveys the basis for the existence and development of accounting and contends that taking accounting as an independent discipline, i.e. the one whose basic principles are not derived from any other disciplines, is unrealistic and stultifying, and thus a conceptual framework cannot be independently constructed. Mattessich (1995: 3-10) assets that, in an applied discipline like accounting, even if a conceptual framework project could be launched with the extensive research that preceded it in academia, it may not be successfully handled in practice. The discussions involved in this thesis are not aimed at agreeing or disagreeing on the aforesaid viewpoints, but at trying to examine those issues in relation to accounting, chiefly the question of what is accounting from another perspective (primarily of accounting). This thesis has devoted a lot of space to review what conceptual framework and its role are, this is primarily because this writer considers that conceptual framework features prominently in both accounting practices and accounting theory, illustrations cited in this chapter may show that many issues relating to accounting have connection with conceptual framework. There is a good quantity of discussions about conceptual framework in international accounting research and standard formulations, however, the contents of conceptual framework in Chinese accounting standards are scarce. From that point, the gap between Chinese accounting and international accounting could be noted.

The research question of this thesis is the possible application of international accounting standards in China, what is argued in the previous parts of this chapter mostly shows that: from the fact that the IASB Framework is used to explain and support IFRSs, it could be noticed that there is the concept of considering conceptual framework in IASB GAAP; from the fact that there is not any explanation about how Specific Standards are connected with the 2006 Basic Standard in Chinese GAAP, it could be manifested that the existing Chinese GAAP does not possess the concept of considering conceptual framework. As a result, one possible argument is that because there is no the concept of considering conceptual framework in Chinese accounting, international conceptual framework cannot be adopted in China; another possible argument is that just because there is no the concept of considering conceptual framework in Chinese accounting, international conceptual framework should be adopted in China. Relating to the notion of 'Chinese learning as basis and west learning for application' shown in chapter 2 of this thesis, what is introduced into China by adopting international conceptual framework should be the 'basis', that is, the concept of considering conceptual framework, but should not be merely the 'application', that is, accounting techniques. In practical work, the application of the common conceptual framework, which is being developed jointly by the FASB and the IASB, could be considered. From the excerpt from an exposure draft of the common conceptual framework on pages 67 and 68, it could be observed that the common conceptual framework is much more profound than the 2006 Basic Standard. Surely, that does not mean that the common conceptual framework is unproblematic, because not only there is controversy over its contents (for example, the discussion on page 93), but when the conceptual framework joint project could be generally completed is still indefinite (to some extent, that could provide a chance of gradually introducing it into China). Once the common conceptual framework has been adopted, it could be used to explain specific standards, and those relative explanations could be displayed in the specific standards, in effect, that is also in accordance with the current stipulations in Chinese GAAP, i.e. specific standards should be formulated in accordance with a conceptual framework (once mentioned on page 103). At this point, one issue which should be raised is that the process of explaining is bound to give rise to contention, for the time being, why there is not yet any contention arising is because there is not yet any explanation so far; even if there is controversy in future, it not only could improve Chinese GAAP through constructive discussions, but also could provide a Chinese angle for the creation of and the improvement to the common conceptual framework. It is mentioned at the beginning of this chapter that a conceptual framework could be considered a system of objectives and fundamentals, or to say, a set of accounting principles (certainly, this description does not mean conceptual frameworks are internally consistent), the concept of considering conceptual framework could be thought of as the concept of considering accounting principles. When the concept of considering conceptual framework, or to say the concept of considering accounting principles, has been introduced into Chinese accounting (and other conditions have been satisfied as well), the direct application of IFRSs in China will become a natural matter.

Finally, another issue in Chinese GAAP deserving of attention is that the ASBEs are such arranged as: a 11-page and 50-Article [the 2006] Basic Standard taken as a conceptual framework; about 400 pages 38 Specific Standards including their implementation guidance; a 142-page appendix, the contents of which are concerning the same as its title, namely, 'a chart of accounts and rules on the recording of transactions'; and 'expert council opinions on implementation issues of ASBE' which is published at irregular interval and 3 issues in total to 2009, and those opinions are mainly for the technical problems arising in accounting practices. The foregoing regulations are all incorporated in Chinese accounting standards, that is, the ASBEs or Chinese GAAP, and are equally effective (note: that is different from IASB GAAP, which explicitly confirms that Guidance on Implementing is not a part of a standard; certainly, similar names do not mean similar comparisons between them). Articles in Specific Standards are very brief, apart from providing the definitions of the relative terms, they just give descriptions of how to do accounting treatments, and this point could be exemplified by Article 11 of ASBE 21 cited on page 94. The implementation guidance of Specific Standards normally has several pages, and not every Specific Standard takes in implementation guidance, and their main contents are supplementary explanations for the implementation of the terms and accounting treatments in accounting practices. For example, the main body of the leases standard ASBE 21 (see pages 93-95) comprises 8 Chapters, 39 Articles in 9 pages (it seems that every Article is not too long), and the titles of the eight Chapters sequentially are: General Provisions, Classification of Leases, Accounting Treatment for Lessees of Finance Leases, Accounting Treatment for Lessors of Finance Leases, Accounting Treatment for Lessees of Operating Leases, Accounting Treatment for Lessors of Operating Leases, Sale and Leaseback Transactions, and Disclosure, it is clear that most of the standard are concerning how to do accounting treatments; the implementation guidance on ASBE 21 has 3 pages, and some of its contents in relation to a further explanation about the classification of leases in practice are cited on page 96. The longest Specific Standard is ASBE30 *Presentation of Financial Statements*, its main body comprises 35 Articles in 10 pages, and its implementation guidance 46 pages, putting the two parts together, 56 pages. ASBE30, together with ASBE 31 *Cash Flow Statements*, stipulates in detail the format of financial statements, including the format of all the notes of financial statements, there is not similar contents in IASB GAAP. (Compared to IAS 7 *Cash Flow Statements* which also allows the indirect method, ASBE 31 only allows the use of the direct method for reporting cash flows from operating activities, along with a note (whose format is stipulated in detail) showing the reconciliation of profit to net cash flow from operating activities using the indirect method.) Apart from that Chinese GAAP stipulates in detail the format of financial statements (including notes), the most distinct difference between Chinese GAAP and IASB GAAP could be that Chinese GAAP contains a chart of accounts, and prescribes very detailed bookkeeping rules on the recording of transactions. Even if those bookkeeping rules are included in appendix, first, appendix is also a part of Chinese GAAP and equally effective as Specific Standards, more importantly, those bookkeeping rules (the above mentioned appendix including them has 142 pages) provide much more details than Specific Standards, to take an example of leases accounting above mentioned, the relative accounting treatments for a lease transaction could be done if without referring to the standard ASBE 21 but just according to the contents in appendix. To sum up in short, a newly identified difference between Chinese GAAP and IASB GAAP at the end of this chapter is that there is a stipulation of detailed bookkeeping rules in Chinese GAAP, the possible reason for this difference will be examined in chapter 6. The next section will discuss the use of fair value in Chinese accounting.

6. a discussion of fair value

The following is an excerpt from the 2006 Basic Standard:

> Chapter 9 Accounting Measurement
>
> Article 41 In recording accounting elements that meet the recognition criteria in the accounting books and records and presenting them in the accounting statements and the notes (hereinafter together known as 'financial statements'), an enterprise shall measure the accounting elements in accordance with the prescribed accounting measurement bases.
>
> Article 42 Accounting measurement bases mainly comprise:
>
> (a) Historical cost: Assets ate recorded at the amount of cash or cash equivalents paid or the fair value of the consideration given to acquire them at the time of their acquisition. Liabilities are recorded at the amount of proceeds or assets received in exchange for the present obligation, or the amount payable under contract for assuming the present obligation, or at the amount of cash or cash equivalents expected to be paid to satisfy the liability in the normal course of business.
>
> (b) Replacement cost: Assets are carried at the amount of cash or cash equivalents that would have to be paid id a same or similar asset was acquired currently. Liabilities are carried at the amount of cash or cash equivalents that would be currently required to settle the obligation.
>
> (c) Net realisable value: Assets are carried at the amount of cash or cash equivalents that could be obtained by selling the asset in the ordinary course of business, less the estimated costs of completion, the estimated selling costs and related tax payments.
>
> (d) Present value: Assets are carried at the present discounted value of the future net cash inflows that the item is expected to generate from its continuing use and ultimate disposal. Liabilities are carried at the present discounted value of the future net cash outflows that are expected to be required to settle the liabilities within the expected settlement period.
>
> (e) Fair value: Assets and liabilities are carried at the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.
>
> Article 43 An enterprise shall generally adopt historical cost as the measurement basis for accounting elements. If the accounting elements are measured at replacement cost, net realisable value, present value or fair value, the enterprise shall ensure such amounts can be obtained and reliably measured.
>
> (extracted from the 2006 Basic Standard)

In contrast to the previous accounting regulations, one of the prominent changes in the 2006 ASBEs is the wide application of fair value. For instance, the accounting standards referring to financial instruments (note: there are three ones altogether, namely, ASBE 22 *Recognition and Measurement of Financial Instruments*, ASBE 23 *Transfer of Financial Assets*, and ASBE 24 *Hedging*, the accounting treatment specified by them is identical with

IAS 39) lay down that all financial assets and financial liabilities should be measured at fair value at initial recognition (Article 30 of ASBE 22), in addition, after initial recognition, an entity should measure financial assets at their fair values, without any deduction for transaction costs it may incur on sale or other disposal, except for… (Article 32 of ASBE 22). Further illustrations include ASBE 11, which sets down that share-based payment transactions for employee services should be measured at fair value (Article 4 of ASBE 11) and ASBE 3 *Investment Property*, which sets out that investment property may be measured at fair value provided certain criteria are met, in which case fair value changes are reported in profit or loss (Articles 10 and 11 of ASBE 3). All the standards mentioned in the above cases for the first time demand measurement at fair value. There are yet more instances applying fair value into the measurement of transactions: For a business combination not involving entities under common control, the purchase method is required, and the assets and liabilities of the acquired enterprise should be measured at fair value (Article 14 of ASBE 20). Exchanges of non-monetary assets should be measured at fair value unless the exchange transaction lacks commercial substance (Article 3 of ASBE 7). Debt restructurings should be measured at fair value, and gains on debt restructuring should be recognized in profit or loss (Articles 10 and 11 of ASBE 12). Moreover, the accounting standards relating to leases, sale and leaseback, government grants and so forth also require measurement at fair value. There are still some dissimilarities between the fair value requirements in Chinese GAAP and the ones in IASB GAAP, to take one example, ASBE 4 *Fixed Assets* and ASBE 6 (concerning the standard of intangible assets) only permit the cost model for measurement of fixed assets and intangible assets (Chapter 4 of ASBE 4, Chapter 4 of ASBE 6), whereas the relative IAS 16 and IAS 38 in IFRSs also permit the revaluation model (paragraph 31 of IAS 16, paragraph 75 of IAS 38). The summary of the use of fair values in Chinese GAAP can be referred to Pacter (2007).

One point worth taking notice is that, by comparison with the stipulation as to fair value measurements set out in IASB GAAP, Chinese GAAP provides that there is conclusive evidence that fair value can be reliably obtainable, a typical example is the measurement of biological assets. ASBE 5 *Biological Assets* prescribes that biological assets should be measured using the cost model, the fair value model can only be applied when there is conclusive evidence that the fair value of the biological asset can be measured reliably on a continuing basis (Article 22 of ASBE 5). While IAS 41 *Agriculture* requires that the fair value model should be adopted for all biological assets unless the estimate of fair value is clearly unreliable (paragraph 30 of IAS 41). Similarly, ASBE 3 specifies that if there is conclusive evidence that the fair value of an investment property can be reliably determinable on a continuing basis, the fair value model may be used (Article 10 of ASBE 3), but the international standard IAS 40 *Investment Property* does not make the same stipulation (consulting paragraph 53 of IAS 40). To sum up, it could be deemed that the fair value requirements both in IFRSs and the ASBEs show a tendency towards convergence, nonetheless, Chinese GAAP inclines to apply the cost model, and otherwise the requirements for conclusive evidence are unique to Chinese GAAP. The next section will discuss the Chinese accounting law.

7. a discussion of fair presentation

There are the following stipulations in the subsection titled 'Fair presentation and compliance with IFRSs' of IAS 1 *Presentation of Financial Statements* in IASB GAAP:

> 15 Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the [IASB Framework]. The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.
>
> 19 In the extremely rare circumstances in which management concludes that compliance with a requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the [IASB Framework], the entity shall depart from that requirement in the manner set out in paragraph 20 if the relevant regulatory framework requires, or otherwise does not prohibit, such a departure.

20 When an entity departs from a requirement of an IFRS in accordance with paragraph 19, it shall disclose:

(a) that management has concluded that the financial statements present fairly the entity's financial position, financial performance and cash flows;

(b) that it has complied with applicable IFRSs, except that it has departed from a particular requirement to achieve a fair presentation;

(c) the title of the IFRS from which the entity has departed, the nature of the departure, including the treatment that the IFRS would require, the reason why that treatment would be so misleading in the circumstances that it would conflict with the objective of financial statements set out in the [IASB Framework], and the treatment adopted; and

(d) for each period presented, the financial effect of the departure on each item in the financial statements that would have been reported in complying with the requirement.

(extracted from IAS 1)

From these citations, it could be noticed that 'fair presentation' is the most important requirement, and has an overriding status. Such kind of overriding requirement was originated in the UK, the terminology used by which is the 'true and fair view', in the first place, the implementation of the true and fair view in the UK will be discussed below.

(1) the true and fair view in the UK

As a concept arising in the UK, the statutory requirement that company accounts should give a 'true and fair view' was first introduced in the Companies Act 1947, which took the place of the former phrase 'true and correct' (as for the historically evolutionary process of the true and fair view in British accounting, see Chastney, 1975; Rutherford, 1985). The present stipulations are made in the sections 393-397 of the Companies Act 2006, specifically, the 2006 Act introduces two types of individual accounts for companies, one is Companies Act individual accounts, which are prepared in accordance with section 396 (see below), the other one IAS individual accounts, which are prepared in compliance with IASB GAAP; section 396 of the 2006 Act lays down the following requirements:

(1) Companies Act individual accounts must comprise – (a) a balance sheet as at the last day of the financial year, and (b) a profit and loss account.

(2) The accounts must – (a) in the case of the balance sheet, give a true and fair view of the state of affairs of the company as at the end of the financial year, and (b) in the case of the profit and loss account, give a true and fair view of the profit or loss of the company for the financial year.

(4) If compliance with the regulations, and any other provision made by or under this Act as to the matters to be included in a company's individual accounts or in notes to those accounts, would not be sufficient to give a true and fair view, the necessary additional information must be given in the accounts or in a note to them.

(5) If in special circumstances compliance with any of those provisions is inconsistent with the requirement to give a true and fair view, the directors must depart from that provision to the extent

> necessary to give a true and fair view. Particulars of any such departure, the reasons for it and its effect must be given in a note to the accounts.
>
> (excerpted from section 396 of the UK Companies Act 2006)

What repays attention is that despite being viewed as a legal concept, the meaning of the term 'a true and fair view' is not defined in the Companies Act 2006 (in actual fact, nor in any version of the Companies Act). In the mid-1980s, the then UK professional standards setting body, the ASC, asked two leading lawyers, Hoffmann and Arden, for their legal opinions on the true and fair concept (considering they became leading judges later and were conferred baron and baroness, their opinions should be authoritative in some measure). The 1983 Hoffmann and Arden Opinion argues that the question of whether company accounts could give a true and fair view (as required by the Companies Act) can be authoritatively decided only by a court because 'true and fair view' is a legal concept and asserts that the readers of the accounts, including businessmen, investors, bankers and so forth, will expect to receive accounts drawn up using the normal practices of accountants, that is accounts that comply with accepted accounting principles, as a result, compliance with accounting standards is prima facie evidence that the accounts are true and fair (this statement suggests that, in certain circumstances, a true and fair view involves something more than mere compliance with the rules currently in existence). Furthermore, the 1993 Arden Opinion repeats emphasizing that the true and fair view is a dynamic concept, thus what is required to show a true and fair view is subject to continuous update and change (concerning the analysis of those legal opinions, refer to Nobes and Parker, 1991; Flower, 2004b: 111-113). In 2008, Moore, a senior barrister, gave his viewpoint on whether the opinions written by Hoffmann and Arden were still suitable in the wake of the enactment of the Companies Act 2006 and the introduction of international accounting standards. The 2008 Moore Opinion endorses the analysis made by Hoffmann and Arden and confirms the centrality of the true and fair requirement to the preparation of financial statements in the UK, whether they are prepared in accordance with international or UK accounting standards.

Corresponding to the Companies Act, the UK accounting standard, i.e. Financial Reporting Standard (FRS) 18 *Accounting Policies*, makes the following stipulation in paragraphs 14 and 15: 'An entity should adopt accounting policies that enable its financial statements to give a true and fair view. Those accounting policies should be consistent with the requirements of accounting standards, Urgent Issues Task Force (UITF) Abstracts and companies legislation'. 'If in exceptional circumstances compliance with the requirements of an accounting standard or UITF Abstract is inconsistent with the requirement to give a true and fair view, the requirements of the accounting standard or UITF Abstract should be departed from to the extent necessary to give a true and fair view…'. The 2008 Moore Opinion argues that, firstly, although IAS 1 uses 'extremely rare', while FRS 18 'exceptional' to describe the likelihood of compliance with an accounting standard would conflict with the objective of financial statements, both of the wordings should not draw any practical distinction between the circumstances which justify their use. Secondly, since accounting standards have become more detailed, the scope for arguing that non-compliance with relevant accounting standards gives a true and fair view, or achieves a fair presentation, has become very limited. Flower (2004b: 114) gives three examples of the true and fair override: The first one relates to depreciation of fixed assets. SSAP 19 *Accounting for Investment Properties* requires that depreciation should not be charged on properties held by a company for investment purposes, whereas the Companies Act prescribes that all assets with limited economic lives shall be depreciated. And then the UK standard setter applies giving 'a true and fair view' into justifying the disregard of the law (paragraph 17 of SSAP 19). The second is that SSAP 20 *Foreign Currency Transaction* stipulates that transaction gains on unsettled foreign currency loans should be taken to income, but this contradicts the requirements set out in the relevant laws that only profits realized at the balance sheet date shall be included in the profit and loss account. Again, the need to show 'a true and fair view' is cited in justification. The third one is that SSAP 9 *Stocks and Long-term Contracts* makes use of the 'true and fair view' rule to restrict the application of the LIFO method of stock valuation, while LIFO is definitely permitted by the relative laws. The foregoing three cases all could illustrate that the standard setter invokes the 'true and fair view override' to disobey the law (relating to the topic of the true and fair view and regulation in the UK, also refer to Alexander, 1993).

(2) the Chinese accounting law

The fundamental law governing accounting in China is the Accounting Law of the People's Republic of China, which is commonly abbreviated to the Accounting Law. The Accounting Law was first adopted in 1985 by the Standing Committee of the People's National Congress, which is the legislative body in China, and was revised twice in 1993 and in 1999. Article 1 of the Accounting Law presents the aim of legislation as follows: 'This Law is enacted for the purposes of standardizing accounting behaviour, ensuring that accounting documentation is authentic and complete, strengthening economic management and financial management, improving economic results and safeguarding the order of socialist market economy'. The Accounting Law contains seven chapters: general provisions, accounting practice, special provisions on accounting practice of companies and enterprises, accounting supervision, accounting offices and accounting personnel, legal liability and supplemental provisions. Compared with the Companies Act of the UK, there are no detailed provisions in the Accounting Law. Chapter 2 and 3 just make some general and basic provisions for accounting practice. A point claiming attention is that the Accounting Law imposes requirements on account books, accounting vouchers, financial and accounting reports and other accounting documents, but fails to clearly specify the status and role of accounting standards. The ending of this section and the ones of the previous two sections individually display three particularities of Chinese accounting, the next chapter will explore the cause of their formation.

VI A DISCUSSION OF POSSIBLE EXPLANATIONS

From the discussions in the previous two chapters of this thesis, chiefly by contrasting Chinese accounting with international accounting, three particularities of Chinese accounting could be noticed: the first one is that Chinese GAAP prescribes the detailed bookkeeping rules on the recording of transactions (mentioned at the end of section 5, chapter 5), while IASB GAAP does not deal with how to record journal entries; the second one is that a good number of Chinese specific accounting standards require that the precondition for using fair value is that there is conclusive evidence of a reliably obtainable fair value (mentioned at the end of section 6, chapter 5), whereas there are no similar requirements for conclusive evidence in IFRSs; the third one is that the Accounting Law, which was amended after the first accounting standard had been effective for six years (specifically, the 1992 Basic Standard came into force in July 1993, and the Accounting Law was amended in October 1999), does not definitely stipulate the role of accounting standards in regulatory framework of accounting in China, nor mention the term 'accounting standards' even (raised at the end of section 7, chapter 5). The objective of this chapter, as implied in the heading, is to explore the possible reasons for bringing about the above three particularities in Chinese accounting, and further the possible influence exerted by those reasons on the future process of the convergence of Chinese accounting standards and international standards (the convergence is the central topic of this thesis). Out of the representative explanations for a wide variety of and a good quantity of international accounting differences, some will be discussed first.

1. the existing explanations

Nobes (1998), in his paper titled 'Towards a General Model of the Reasons for International Differences in Financial Reporting', examines the usefulness of previously proposed general factors for explaining accounting differences and the logical relationship between those factors. Briefly speaking, he argues that such factors as below are possibly not the causes of major international accounting differences: first, tax (the primary reason is because the dissimilarity that, in some countries, tax rules issued by governments are inclined to dominate accounting systems including financial reporting rules for business enterprises, and in some other countries, the financial reporting rules conventionally differ from the tax rules (certainly that does not mean that there are no tax considerations in accounting practices), could be thought of as a result of the (non-)existence of two sets of rules rather than the major cause of international accounting differences, in other words, even if there is no the tax variable, accounting differences can still exist); second, legal systems (mainly because the legal variable, here specifically indicated as the regulatory system for accounting, e.g. whom the accounting regulations should be formulated by, the professional bodies or the authorities, is dependent on, but not independent off, the financing factor, to take an instance, the importance of investors (specifically, for example, if under the great power of investors, financial reporting rules would be created by accounting profession to embody the requirements of investors for disclosure and presentation, and be separated from tax rules controlled by government)); third, level of economic development (the realities are that the accounting systems of many African countries are similar to the UK's or French accounting system, and Nobes agrees that colonial inheritance is probably the major explanatory factor for the foregoing); and the other possible factors unconnected with international differences, which encompasses level of education, inflation levels, influence of theory, history, geography, language, and so forth, why they are unconnected is mostly because they are either the results of accounting differences rather than their causes, or too broad to be useful for explanations. In spite of the absence of the relative discussion in his paper, Nobes does not absolutely exclude political factors as the cause of accounting differences; as for culture, Nobes holds that it is better to perceive cultural variables as an influence on other variables rather than a direct effect on accounting. Nobes proposes that, at least for the purposes of dividing developed countries into major groups, the most important direct cause of the international differences in financial reporting is a two-way split of countries into: (i) those with important equity markets and many outside shareholders; and (ii) those with a credit-based financing system and with relatively unimportant outside shareholders. The equity/outsider system leads to a separation between tax and accounting rules, and to large auditing professions, is also generally associated with the common law system (as for Nobes' classification, see also Nobes, 2004; Alexander and Nobes, 2004: 80-97). Especially, Nobes (1998; note: what this sentence describes is a prediction made by Nobes in 1998) takes China as an example and states that China is a country without a strong equity market and shareholders tradition, but it seems to be moving towards such an equity/outsider system, and then to be followed by an accounting system focused on accounting for external shareholders. It sounds as though the current situation of Chinese accounting could corroborate Nobes' theory and his prediction of the development of Chinese accounting, especially in the light of the fact that the specific accounting treatments and the finally presented financial statements prescribed in current Chinese and IASB GAAP are broadly the same. To put that in other words, the model proposed by Nobes(1998) could nicely elaborate the entire process of such a development as that the ASBEs are being developed with a view to achieving convergence of IFRSs, nevertheless, it is hard for his model to explain the three particularities of Chinese accounting mentioned at the beginning of this chapter (viz the stipulation about bookkeeping rules, requirements for conclusive evidence concerning the use of fair value, and the undefined legal status of accounting standards). All the same, Nobes' model is only a general one, what it concerns is the major and systematic differences, but not the explanations of relatively small differences (note: here one point claiming special attention is that superficially subtle differences are not generated all by trivial causes, but possibly by considerably significant ones), and what it refers to is mostly the accounting systems of Western developed countries. At last, another point deserving of attention is that: 'At its simplest level, accounting is about the provision of figures to people about their resources' (abstracted from Alexander et al., 2007: 3; note: this sentence is the first one of that book; although that book is especially for the textbook purpose, it is of significantly academic value, firstly because it provides the most mainstream description of accounting; secondly, the first sentence of the book emphasizes both 'people' and 'resources' in accounting, which is of great help with the forming of the main idea of this thesis). It is not difficult to notice that Nobes' (1998) proposed scheme for classification of accounting systems, that is, the division between strong equity class and weak equity class, is primarily on the basis of 'resources' in accounting, but without too many considerations of 'people' in accounting.

Gray (1988), in his paper headed 'Towards a Theory of Cultural Influence on the Development of Accounting Systems Internationally', adopts the cultural model presented by Hofstede (1980, 1983, 1984; note: the paper by Gray was published in 1988, when Hofstede had not advanced the fifth cultural value dimension, i.e. long-term versus short-term orientation; the research by Hofstede is brought into chapter 2 of this thesis), applies cultural differences to explaining international differences in the behaviour of accountants and therefore in the nature of accounting practices. He proposes the identification of four accounting values as follows: professionalism versus statutory control, uniformity versus flexibility, conservatism versus optimism, and secrecy versus transparency; the two former accounting value dimensions principally concern authority and enforcement, and the two latter ones are principally concerned with measurement and disclosure. To employ Gray's theory to specifically survey accounting in China, in cultural terms, China is a society with a high degree of centralization of authority, and Chinese culture entails people conforming with imposed code, but not pursuing original thought and having risk taking attitudes (note:

at this place one thing needing attention is that the Chinese societal values here referred to could be thought of as inconsistent with the meaning of 'culture', the reason for taking them as cultural constraints is because they fall in the scope of the cultural study conducted by Hofstede, and Gray's theory is grounded on Hofstede's theory). Owing to the foregoing Chinese cultural constraints, Chinese accounting, including the accounting profession, tends to be controlled by the government (but that cannot be determined simply by the cultural factor, further discussions will be continued below), the government is apt to enforce (additionally, accountants incline to accept, certainly it is impossible for them to reject) accounting rules which are mandatory, detailed, and uniform, rather than accounting standards which could much more embody flexibility and accounting professionalism, that situation leads to two phenomena that Chinese GAAP incorporates a chart of accounts and detailed bookkeeping rules and that accounting standards are not necessary to be stipulated in the Accounting Law (for they are not important); and in accounting measurement, government deems that, in comparison with fair value, historical cost could more clearly signifies conservatism (mostly because varied historical cost based provisions could be utilized to cope with the uncertainty of future volatility), hence lays down strict requirements for the use of fair value (as to Gray's model, see also Nobes, 2004; Radebaugh et al., 2006: 41-52; in relation to the analyses of Chinese accounting values, refer to Chow et al., 1995). It appears as if the problem raised at the beginning of this chapter had been perfectly expounded by Gray's theory of cultural relevance (surely, the explanation is proposed by this writer, and unable to represent Gray's and other people's possible opinions), however, one point meriting attention is that the other characteristics of Chinese accounting system could be delineated also by Gray's theory, further, even it could be said that any feature of any accounting system could be elucidated by Gray's theory that societal values determine accounting values, and accounting values determine accounting systems and practices (however, this does not mean that Gray's theory is universally applied, but probably because his theory is vague and indirect); those elucidations are, to a great degree, dependent upon how the person who proffers them elucidates (different people could give different explications); that is to say, apart from cultural influence, there could be more explanations which are concerned more closely with the three particularities referred to at the beginning of this chapter, namely more closely with accounting. Finally, one point which will be discussed is that Gray's approach concerning culture is often perceived as vague and indirect when it is taken to explain specific accounting issues (to give an example, the relationship between Chinese societal values and accounting values above indicated by this writer sounds farfetched), the possible reason is that although the people in accounting are affected by culture, they are impossible to be influenced simply by cultural factor, both of political factor and economic factor could become the influential factors in the external environment surrounding the people in accounting (that may be why political, economic, and cultural factors are known as environmental factors); the other point is that because the cultural factor (and other ones) exert influences over people, and people affect accounting (as implied by Gray), the above mentioned possible explanations more closely relating to accounting probably bear relation to people.

Xiao et al. (2004; note: this paper is cited in chapter 2; being differentiated from the foregoing articles referring to the differences in international accounting systems, this one specially deals with Chinese accounting), underline the importance of political influence (from government officials) in Chinese accounting. To put it simply, mainly from interviews with the officials of the Chinese government in charge of accounting (Xiao et al.'s interviewees comprise five accounting regulators at the departmental official rank, three academics, and an auditor), they observes that the Chinese government has persistent, comprehensive, and detailed control over accounting, and what the government pays more attention to is the practical outcome and political effects of the accounting system, for example, to ensure that accounting rules will not affect government revenues or taxation (in the long run), hence the standardized bookkeeping rules weigh more than accounting standards which could reflect more professionalism but less governmental intervention. In other words, from Xiao et al.'s paper, it could be noticed that Chinese accounting regulators, as government officials, could have strong political property and considerations, (in effect, that is the commonly accepted realities in China, and Xiao et al.'s article confirms this point with the method of interviewing government officials, such process of argument might be debatable), probably for the sake of political considerations, regulators prefer creating bookkeeping rules (and adhering to historical costs); however, Xiao et al.'s paper does not provide the concrete opinions held by Chinese accounting regulator about what accounting is.

To make a short summary, the purpose of citing the above three articles is generally to try to answer the question put forward at the beginning of this chapter (that is, the reasons for leading to the below three particularities: the formulation of bookkeeping rules in Chinese accounting, the restriction in the use of fair value, and the undefined status of accounting standards in regulatory framework) in economic, cultural and political terms, although the three articles could propose some explanations, they do not proffer direct elucidations from the perspective of accounting, and do not explicate the three particularities as a totality. In spite of that, the foregoing analyses manifest that people's dissimilar conceptions of accounting could be employed to explain the differences between accounting systems (this viewpoint is presumably inferred from the argument that accounting is created by people, therefore the dissimilarities existing in accounting should fundamentally relate to people's different conceptions of accounting); and in view of the fact that Chinese accounting regulators can predominantly decide on and decisively participate in Chinese accounting, some factors relating to them could be a crucial key to answering the question raised at the beginning of this chapter. The following is an alternative view on the question.

2. an alternative view

(1) step one

The following contents are referred to in the process of argument in chapter 3: Schipper (2003) holds that the FASB's standard setting activities are guided by SFACs, viz the US conceptual framework, and then US GAAP is generally based on the principles incorporated in the US conceptual framework. In opposition to the above opinions, Nobes (2005) believes that quite a few existing standards embrace extensive rules and optional accounting methods, this situation stems from standards which lack principle or are grounded on inappropriate principles. Solomons (1989, reprinted in 1997) deems that developing conceptual frameworks could help standard setters set and revise specific accounting standards. As an opposition of Solomons' argument, Macve (1981, 1983a, reprinted in 1997) regards that conceptual frameworks could not be of help with resolving individual accounting issues, the purpose of standard setters formulating those frameworks is to cope with the political interference in the process of standard setting. It could be observed that there is a common point among those mentioned academics, that is, all of them are contemplating accounting principles in their discussions. Chapter 4 of this thesis views that there is the concept of considering conceptual framework, or to say, the concept of considering accounting principles in IASB GAAP (or in other words, IASB GAAP setters take accounting principles into consideration). As far as Chinese accounting is concerned, even if there is a conceptual framework in Chinese GAAP, i.e. the 2006 Basic Standard, the 2006 Basic Standard is never referred to in the body of specific standards (except being mentioned once in Article 1 of each specific standard), let alone being applied to explaining and upholding specific standards, moreover Chinese GAAP provides the detailed bookkeeping rules, from this point, it could be shown that there is the concept of 'do bookkeeping' in Chinese accounting (that could mean what Chinese accounting standard setters are thinking over inclines to be 'do bookkeeping').

The discussion in section 6 of chapter five is concerned with the following subject matter: Edwards and Bell (1961) set forth an array of value concepts, put forward CVA, an entry value model of measurement, and point to that CVA can provide more meaningful information (in comparison with current exit value data) about an entity in continuing operation. Chambers (1966) formulates CoCoA, an exit value framework, and regards that his system can offer an indication of an important opportunity facing an entity, that is whether it could be better off in an alternative form. Baxter (1967) advocates value to the owner, which is a concept of combining alternative valuation methods, and believes that value to the owner can provide a principle for selecting the most defensible type of current value for each kind of asset and liability. It could be discerned that the above academics share a common point, namely, they all take value into consideration in their expositions. Chapter 5 of this thesis judges that there is the concept of considering value in IASB GAAP, especially from a developmental perspective. With regard to Chinese accounting, the whole Chinese accounting system is historical cost based, only under the circumstances of 'conclusive evidence' could fair value become an alternative to historical cost, in addition, only some of accounting standards allow that alternative, and the historical cost's connection with a natural number is much closer than the one between it and value, as a result, it could be concluded that there is the concept of 'record a number' in Chinese accounting (or to rephrase it, Chinese accounting standard setters have a tendency towards taking account of 'record a number'; but drawing the above conclusion seems not persuasive enough merely according to the above grounds, this issue will be further elaborated later).

In section 7 of chapter 5, the following subject matter is discussed: Alexander (1999, 2001) takes the view that the true and fair view should be the fundamental criterion for financial reporting, and the true and fair override could be employed by preparers of financial statements to deal with special cases in a dynamic economy. Nobes (2000) is of the opinion that preparers could misuse the true and fair override, and an override should not be included in standards. Walton (1993) holds his viewpoint that the true and fair view in British accounting practice could be interpreted as a code word for GAAP. It could be noticed that all of the above-mentioned scholars bear a similarity, namely, they all take professional judgment into consideration in their explications. Chapter 5 of this thesis suggests that there is the concept of considering professional judgment in IASB GAAP. In terms of Chinese accounting, the Accounting Law provides that accounting vouchers, account books, financial and accounting reports and other accounting documents must conform to the provisions of the uniform accounting system, and must be authentic and complete. In effect, authentic and complete accounting vouchers would not surely give rise to ‘authentic and complete’ financial statements, while accounting standards and professional judgment feature prominently in the process of preparing financial statements, but the Accounting Law refers to no accounting standards whatever even. From that fact, it could be revealed that what the Accounting Law puts emphasis on is the procedure in accounting practice, so it could be assumed that there is the concept of ‘follow procedure’ in Chinese accounting (put it in other way, Chinese accounting regulators, who are standard setters as well, lean towards consideration of ‘follow procedure’).

(2) step two

Any concept of accounting is people’s concept of accounting. As above stated, there is the concept of considering accounting principles, value, and professional judgment in IASB GAAP, or it could be written out as there is the concept of ‘principle, value, judgment' in IASB GAAP, alternatively, the setters of IASB GAAP have the concept of 'principle, value, judgment'. By contrast, there is the concept of 'do bookkeeping', 'record a number', and 'follow procedure' in Chinese accounting, or it could be believed that Chinese accounting standard setters have the concept of 'just bookkeep a number' (note: the verb 'bookkeep' is intransitive according to grammar, such use here is for the sake of writing conveniently, but is not grammatical). One person cannot have three concepts of accounting, so 'just bookkeep a number' could be taken as a totality (the 'principle, value, judgment' in IASB GAAP could also be taken as a totality). To take the concept of 'record a number' above discussed as an example, in contrast to historical cost, the application of fair value entails professional judgment, and is hard to be regulated by employing bookkeeping rules, therefore, 'value' commonly forms a totality together with 'principle' and 'judgment', whereas 'record a number' is usually connected with 'do bookkeeping' and 'follow procedure' (here one point which should be stressed is that not all of the connections in the totality could be reflected in accounting standards, because the process of accounting standards setting are affected by a lot of other factors; to a great extent, it is the people in accounting could have this kind of concept of accounting). To sum up, this thesis, by the analyses of (documents of) Chinese accounting standards and its regulatory framework, reaches the below conclusion that the concept of accounting possessed by Chinese accounting regulators, who are also accounting standard setters, is 'just bookkeep a number'.

Although Chinese GAAP is basically consistent with the specific accounting treatments in IASB GAAP, the analyses in this thesis could exhibit that the concept of accounting on which Chinese accounting is grounded is different from the one international accounting is based on, specifically, IASB GAAP could be thought of being derived from the concept of 'principle, value, judgment', while Chinese GAAP could be considered being stemmed from the concept of 'just bookkeep a number'. The difference in the concept of accounting could likewise answer the question raised in chapter 1, i.e. ‘what could be the reasons why international standards cannot be directly applied presently in China’. Taking government grants related to assets as an example (mentioned on page 6, 7, 55 and 56), in the stipulations prior to ASBE 16 coming into force, the total amount of the assets related grants should be recognized as capital reserve, whereas ASBE 16 requires that the grants should be recognized as deferred income and reported as income evenly over the useful life of the asset (Article 7 of ASBE 16; besides, in contrast, paragraph 26 of IAS 20 allows the presentation of the grants as deferred income, and their recognition as income on a systematic and rational basis over the useful life of the asset). This instance shows that the change from the former GAAP to the latter GAAP is from the grant being credited to the ‘capital reserve’ account to being credited to the ‘deferred income’ account and being debited evenly in subsequent years (i.e. the alteration in account books and journal entries); as to whether that grant is a liability or not, and what the figures which are reported as income mean, that kind of questions are not within the scope of consideration (actually there is no need to take account of them). The present convergence of Chinese accounting and international accounting is displayed by ‘application’, i.e. accounting techniques, but not by ‘basis’, i.e. the concept of accounting, at least, not by the ‘basis’ that Chinese accounting regulator to take as. Admittedly, the difference which exists ever in the concept of accounting does not mean it will last forever, or will never been eliminated, next chapter will explore the possibility of convergence of concept, that is, the ‘possible’ in ‘the possible application of international accounting standards in China’.

VII THE ACCOUNTING PROFESSION AND ACCOUNTING ACADEMICS IN CHINA

From chapter 4 to 6, this thesis makes some analyses of Chinese accounting standard setters (they are also Chinese accounting regulators) by discussing Chinese accounting standards and regulatory framework for accounting. It is noticeable that the other important participants in Chinese accounting comprise the accounting profession and accounting academics.

1. Chinese accounting profession

The following is a brief historical background to the Chinese accounting profession: In the early 20th century, in tandem with the quick development of shareholding companies and the resultant increased demand for external auditing, the Chinese certified public accountants (CPA) profession was established and private CPA firms and societies were founded to cater for that situation. After the CPC took power in 1949, along with the swift and total elimination of the private ownership, the CPA profession had vanished because of the closing of CPA firms and the substitution of government audit for it, specifically, the CPA profession was replaced by a system of ‘specialist supervision and internal accounting control’ (and all of accountants in China became government employees). The economic reform since 1979 resulted in the rapid expansion of Sino-foreign joint ventures, foreign investors preferred to employ an accounting firm, instead of governmental auditors, to perform the audit of annual financial statements, income tax returns, and the like. In the early 1980s, in order to meet the needs of the foreign investors, the MOF announced provisional regulations and then the CPA profession and accounting firms re-emerged. In 1986, the State Council promulgated the CPA Regulations, which prescribed the scope of CPA practice and some working and ethical rules. The CPA Regulations and CPA’s development in those days led to the formation, in November 1988, of the CICPA, a nominal professional accounting body, which is under the jurisdiction and close supervision of the MOF. On behalf of the MOF, The CICPA assumes the responsibility of addressing routine affairs relating to CPAs, such as monitoring the operations of CPA firms, organizing and carrying out CPA training programmes, arranging and implementing the national CPA examinations, and so on. In 1993, the CPA Law was enacted (to substitute for the CPA Regulations) and empowered the MOF to issue audit standards. Those standards are closely modeled after International Standards on Auditing issued by the International Federation of Accountants. Further economic reforms, including the opening of securities exchanges and the establishment of shareholding companies, substantially relied on CPA services and correspondingly stimulated the growth of the CPA profession. In order to alleviate the shortages of CPAs, the first national unified CPA examination was held in 1991. Before the CPA examination, all CPAs were certified as different professional grades according to their experience and educational background by regulatory authorities through an evaluation system. The second CPA examination was held in 1993 and the examination became an annual event. From 1995 onwards, to qualify as a CPA, a candidate must take a set of five examinations (including accounting, auditing, financial cost management, economic law, and taxation law), and after passing all of the five exams, the candidate must obtain at least two years of work experience in accounting or auditing (as for the developmental history of public accountants in China, see Mo et al., 1995; Dai et al., 2000; DeFond et al., 2000; Xiao et al., 2000).

Subsequent to the revival of the CPA profession in the 1980s, the problems arising in its developmental process mainly included professional competence and audit independence owing to the historical causes (namely, CPA services had been held in abeyance for more than 30 years) and the institutional causes (in particular, the government had played a predominant role in the development of the profession, there are further discussions on that topic below). As for the professional competence issue, a great number of the older generation of CPAs did not receive systematic professional training and academic education, nor had adequate experience with market economy transactions, for example, some CPAs simply considered an audit as a check on whether financial statements were consistent with the ledgers (Xiao et al., 2000). 'Since the introduction of the professional examinations, a large number of young CPAs have joined the profession. They are usually college graduates with limited work experience…to assume management positions.… In summary, ageing members, outdated knowledge, lack of continuous professional education and a lack of familiarity with emerging business activities in a market economy account for the professional inadequacy of many CPAs in coping with the ever-increasing demand for CPA services' (Tang et al., 2003: 197). The more important issue is that the independence of auditors should be improved in China. As stated above, the CICPA, which attempts to promote its image as a non-governmental regulatory organization of the CPA profession, actually operates under the direct supervision of the MOF, with its president, vice-president, and most of the council members being appointed by the MOF. These officials have a background in government services rather than in accounting and auditing. Government officials regard CPA services as a mere supplement to the government control and its extension. In the supervisory framework, only the MOF have the power to approve the establishment of accounting firms, maintain a register of CPAs (that means that CPAs are under the control of the government, not of the CICPA), formulate rules and procedures of the CPA examination, approve the practising standards and rules proposed by the CICPA, and so forth; whereas the CICPA's authority is limited to assisting the MOF (in organizing examinations and something of that description, as above mentioned). In order to administer the national CPA examinations, there is an Examination Department that is subordinate to the CICPA, it and the Office of the CPA Examination Committee of the MOF are actually one unit, but have two names, and are headed by a deputy minister of the MOF (relating to the CICPA and professional (self-)regulation, see Graham, 1996; Tang et al., 2003: 160-163, 196-198). The other problem of auditor independence appearing in the development of the Chinese CPA profession is that many CPA firms were/are government-affiliated. In a period of time following the restart of the CPA profession, most CPA firms were established with sponsorship from government agencies, that arrangement was helpful for those firms to gain capital, sources of business and legal protection. What is more, being motivated by the high profitability of accounting firms, governments at all levels promptly set up accounting firms to increase their revenue, their usual practices are exercising their administrative authority to refer enterprises under their jurisdiction to their own CPA firms for audit and related services. Evidently, the interference and protection from government agencies caused unfair competition among CPA firms, impaired the professional independence of CPAs, and could result in lower quality of services. There were also some public accounting firms to be attached to universities, they provided university staff and students with the opportunities of acquiring practical experience, at the same time, brought a source of revenue to universities. From 1997 onwards, the MOF required all CPA firms to sever the link with their sponsoring government agencies and be restructured as partnerships with limited liabilities or as corporations. It could be easily understood that there was enormous resistance to the restructuring from both government officials and accounting firms, because cutting their ties with the government meant accounting firms lost a steady flow of business, while as far as government agencies were concerned, they suffered the loss of income generating units. Apart from Chinese firms, international firms, for instance the Big Four, were allowed to operate in China in the form of joint ventures with local firms, the authorities expected them to assist local accountants to enhance their professional standards. The size of the business handled by those international firms has been quickly increasing (concerning the hooking-up of Chinese CPA firms and other issues, refer to Dai et al., 2000; Tang et al., 2003: 158-169, 197-202).

Although the literature directly referring to what the Chinese accounting profession's opinions on accounting are is very few, it could still be considered that the contents incorporated in the Chinese CPA examination might be taken as a proxy for aiding to answer the above question. The Chinese CPA examination was reformed in 2009, and its present form is as follows: the examination is held once a year and divided into two stages. The first stage is professional and consists of six papers, namely accounting, auditing, financial cost management, economic law, taxation law (the names of the five papers are the same as prior to the reform), and the newly added business strategy and risk management; the passing of any paper in the first stage is valid for five years. A candidate who can successfully pass all of the above six papers within five years will be granted a certificate of the first stage and entitled to the examination of the second stage, which is comprehensive and only includes one subject, i.e. the test of professional ability. A candidate who succeeds in passing the examination of the second stage within five years can be awarded a complete certificate, and then the candidate must apply to join the CICPA, otherwise, the certificate will expire beyond five years. A candidate who is working in an accounting firm and possesses two years' experience in auditing and the complete certificate can be certified as a practising CPA, while a candidate who only has the complete certificate can be certified as non-practising CPA. The below is an additional question in English (except it, the whole paper is in Chinese) of the 'Accounting' paper of the 2009 CPA examination (that was the last examination before the reform) and is put at the end of the paper.

In 20×8, the following events related to Entity A were noted:

(1) Entity A sells goods with a warranty under which customers are covered for the cost of repairs of any manufacturing defects that become apparent within the first twelve months after purchase. If minor defects were detected in all products sold, repair costs of RMB 2,000,000 would result; if major defects were detected in all products sold then repair costs of RMB 6,000,000 would result. Entity A's past experience and future expectations indicate that, for the coming year,

60 per cent of the goods sold in 20×8 will have minor defects and 10 per cent of the goods sold in 20×8 will have major defects.

(2) In November 20×8, a customer sued Entity A and made a claim for damages of RMB 2,500,000, as Entity A failed to deliver the goods to the customer in time according to the delivery term of relevant sales contract. When Entity A prepared the financial statements for the year ended 31 December 20×8, its lawyers advised that it was probable that Entity A would be found liable for making a payment of RMB 2,000,000 to the customer for compensation.

(3) Under new environment protection legislation, Entity A is required to fit smoke filters, which cost about RMB 20,000,000, to its factories by 30 June 20×8. Entity A has not fitted the smoke filters at 31 December 20×8. Based on the best estimate of the management of Entity A, it is more likely that Entity A will be imposed a penalty of RMB 10,000,000.

(4) Entity A is required by law to overhaul its equipments once three years. The estimated remaining useful life of the equipments is 18 years. Entity A just spent RMB 6,000,000 in overhauling its equipments in 20×7.

(5) Entity A entered into a sales contract with a customer in November 20×8 to sell equipment at the price of RMB 50,000,000. According to the sales contract, Entity A shall deliver the equipment to the customer in the end of 20×9 and the amount of penalty is RMB 6,000,000 if Entity A or the customer fails to fulfill the contract. Entity A's original estimated cost of fulfilling the sales contract is about RMB 45,000,000. However, due to the increase of the purchase prices of relevant raw materials, the estimated cost of fulfilling the sales contract has increased to RMB 55,000,000 in the end of 20×8. No inventory has been prepared by Entity A for the production of the equipment by the end of 20×8.

Required:

According to the events described above, determine whether any provision should be recognized in Entity A's financial statement for the year ended 31 December 20×8. If any provision should be recognized, calculate the amount of provision and prepare related journal entries.

A suggested answer is as follows:

(1) The provision should be recognized.
Dr Sales expenses 1,200,000
Cr Provision 1,200,000

(2) The provision should be recognized.
Dr Non-operating expenditures 2,000,000
Cr Provision 2,000,000

(3) The provision should be recognized.
Dr Non-operating expenditures 10,000,000
Cr Provision 10,000,000

(4) The provision does not have to be recognized.

(5) The provision should be recognized.
Dr Non-operating expenditures 5,000,000
Cr Provision 5,000,000

(extracted from the Accounting paper of the 2009 Chinese CPA examination)

(note: The above 'RMB' is the abbreviation for the Renminbi (its literal meaning in Chinese is people's currency), which is the official currency of China, and whose principal unit is the Yuan; 'Dr' and 'Cr' are the symbols used by the double entry system, respectively indicating making a debit entry or a credit entry in the account.)

One point which should be emphasized is that the last question in English does not involve complex journal entries, or to say, it might be the simplest of all the questions in the paper, because it is primarily aimed at testing the examinees' level of English. A lot of questions included in the Accounting paper are much more difficult to answer than the above cited question, but all of them, like that one, just require preparing journal entries, for instance, two comprehensive questions preceding that question in English need making a great deal of journal entries of adjustment and offsetting, together with a fair amount of calculations, for the comprehensive business transactions of an entity. From the perspective of accounting, the question above quoted is for the recognition and measurement of provisions. Like the stipulations presented by the current IASB GAAP mentioned in the section 4 of chapter 3, ASBE 13 specifies that an entity should recognize the related obligation of a contingency as a liability when the following conditions are satisfied: (1) that obligation, which can be either a legal obligation or a constructive obligation, is a present obligation from past event, (2) a probable outflow of economic benefits will be required to settle the obligation, and (3) a reliable estimate can be made of the amount of the obligation (Article 4 of ASBE 13). The amount recognized as a provision should be the best estimate of the expenditure required to settle the present obligation… (ibid, Article 5). If an entity has a contract that is onerous (an onerous contract is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it), the present obligation under the contract should be recognized and measured as a provision (ibid, Article 8). Provisions should not be recognized for future operating losses (ibid, Article 9). Although that question is concerning the examination of the above mentioned articles in ASBE 13, what it underlines is doing bookkeeping instead of observing problems from the angle of accounting principles such as the definition of a liability. Moreover, there is no need for considering whether more liabilities will appear on the balance sheet once Chinese GAAP has adopted in future the IASB's revision to IAS 37 (note: the IASB's exposure drafts are mentioned on pages 106 and 107, here just as a reminder, the staple of which is about the cancellation of the idea of provisions or contingent liabilities and the requirements that an entity should recognize an item as a liability if the item meets the definition of a liability and the entity can measure the liability reliably), and whether it will be appropriate to use the amount that an entity would rationally pay at the end of the reporting period to be relieved of the present obligation to measure a liability (certainly, the 2009 examination is previous to the 2010 exposure draft). To make a brief summary, the whole of the Accounting paper, including all of the papers of the past years, arguably lays the focus of the examination on how to do bookkeeping; however, in effect, accounting could be much richer in contents than bookkeeping, so it might be doubted whether the examinees, or those who are interested in accounting, under the influence of the Chinese CPA examination which is pragmatically viewed as crucial for employment and promotion, could consider the bookkeeping's principle of that 'each transaction consists of debits and credits, and for every transaction they must be equal' to feature prominently in accounting. At this place, there is one point deserving attention that those examination papers are prepared by the Office of the CPA Examination Committee of the MOF, hence it could reflect (more appropriately speaking, could more reflect) what Chinese accounting regulators expect Chinese accountants to learn and master is. Incidentally, it could be thought that the three particularities in Chinese accounting mentioned in the early part of chapter six can be explicated by utilizing the factor of age and size of accounting profession (see Nobes, 1998); in practical terms, because the Chinese accounting profession is rather young and weak, the detailed bookkeeping rules are stipulated (to ensure that the correct journal entries are recorded), and the estimates in valuation are used to a minimum. However, as for the above mentioned, it should be stressed that, first of all, Chinese accounting profession is controlled by accounting regulator, and more importantly, in historical and developmental terms, it is the accounting regulator's but not the accounting profession's accounting concepts that determine the features and developmental tendency of Chinese accounting.

2. Chinese accounting academics

Another major participant in Chinese accounting is accounting academics. The Accounting Society of China, a national academic organization, was formed in 1980 and is directly managed by the MOF, and its journal, Accounting Research, financed by the MOF and edited by the MOF officials. Tang (2000) believes that accounting academics have been catalysts of the movement towards modernization and internationalization of accounting in China, for example, according to his statistics, during the period between 1980 and 1997, there are 222 articles in Accounting Research devoted to introducing, explaining and analyzing the development and research results of Western accounting, and those articles greatly helped in reaching the consensus of adopting international accounting practices. While at the same time, Gao (1995), Ji (2000), and Tang (2000) also notice that political accounting lies in the area of accounting research. Many accounting researchers in China are under the influence of Marxism theory and prefer ideological debate; they behave simply as propagandists for the CPC, socialist ideology and government policies. Government officials make use of accounting journals as a forum to promote their policies, to give an example, over the above mentioned period of time from 1980 to 1997, Accounting Research, which had been highly expected as a pure academic journal, published 250 politically oriented papers as well as speeches by Communist and government officers, which were usually considered to provide the theoretical background to accounting research in China. In recent years, the speeches by the Party's and government's officials in Accounting Research have become less than before, but those speeches are viewed as having a guiding role in academic researches, as evidenced by the fact that none of the academic papers published in Accounting Research has ever expressed different opinions from the superiors' speeches. Another possible phenomenon claiming attention is that most of articles in that journal are concerned with the introductions to and evaluations of international accounting standards and research results, and keep indicating flaws in international standards and researches and places where further improvements could be made; the articles relating to the study on China just make up a minority of Accounting Research, an journal published in China, and nearly always prove both ongoing and oncoming accounting standards to be completely reasonable. Moreover, since China's accounting system began changing towards a gradual convergence with international accounting standards, Western accounting scholars have shown increasing interest in Chinese accounting, and China has sent a number of accounting scholars to developed countries to learn advanced accounting techniques and theory. Most of leading international accounting journals have published papers on Chinese accounting issues, of which many were written jointly by Western and Chinese accounting academics working in collaboration. These articles provided up-to-date information about Chinese accounting developments (Ji, 2000). Here there is a possible fact meriting notice that plenty of articles published in international journals have discussions about the influences on Chinese accounting exerted by environmental factors, however, none of articles analogous to the papers published overseas has ever appeared in Accounting Research (as for the reason, it is very probably because of the effects of environmental factors).

To sum up, as far as the accounting profession and accounting academics, two of the main participants in Chinese accounting, are concerned, on the one hand, the possible application of international accounting standards in China involves the accounting profession being able to have its own independence and accounting academics being able to express their opinions freely; on the other hand, both of them are controlled on a great level by accounting regulators. The next section will review the developmental history of Chinese accounting.

3. a brief summary

Chapter one of this thesis raises a question of 'what is the feasibility of fulfilling the direct application [of international accounting standards in China] in the future', from the discussion in this chapter and chapter 3, it could be clarified that the key to the above question is the thinking of Chinese accounting regulators, as they, on a considerable level, determine the Chinese accounting profession and accounting academics; China's economic development could drive the reform of accounting, but being attributed to China's characteristics, it serves for politics to a great extent and the political concept possessed by Chinese accounting regulators would decide the future direction for the development of Chinese accounting. Nevertheless, all in all, one point which must not be neglected is that everything in China, certainly including accounting and accounting regulators, is governed by the CPC.

VIII CONCLUSION AND FURTHER DEVELOPMENTS

The research question of this thesis is the possible application of international accounting standards in China, on which all of the previous chapters have had discussions from different perspectives. The discussion about the context of Chinese accounting in chapter 3 could show that China lacks such elements in the context of IFRS as capital market, corporate governance, independent accounting profession, civil society with the rule of law and so forth. Chapter 4 and chapter 5 chiefly research the relevant issues concerning the conceptual framework aspect of accounting, the references to which are relatively insufficient in Chinese accounting standards, that reveals the divisions between Chinese standards and international standards. As have been discussed in chapter 6, this writer is of the opinion mainly that China should introduce the 'basis' of international accounting standards, that is to say the concept of accounting, including principle, value, judgment (and other factors, details are discussed below), rather than the mere 'application' of accounting techniques incorporated in international accounting standards. Convergence of Chinese accounting standards and international standards should be an outcome of the convergence of the concept of accounting. At the same time it needs to be noted that the process cannot be fulfilled merely by accounting per se, the development of accounting, including convergence, is eventually determined by the context they are set in. It could be perceived that the topic of the adopting of international accounting standards in China would be senseless until China has had such factors as rule of law, corporate governance, capital market and so on. Certainly, as stated in chapter one, this thesis is just a personal opinion of this writer, and how to converge is a matter for the Chinese accounting regulators to determine. It is noticeable that the factors Chinese accounting regulators should take account of are not simply concerned with accounting by any means, but even more intricate. Thus far, the research question of this thesis has been already answered, and the following are two topics that may need further discussion.

The first one relates to accounting ethics. In spite of no literal mention of ethics in IASB GAAP, the application (and creation) of IASB GAAP (ought to be the application (and creation) of any GAAP) must involve ethics. (It is difficult to give an exact definition of 'ethics', by and large, ethics is concerned with right or wrong, good or bad; this topic can be referred to Duska and Duska (2003: 24-64).) Taking the accounting issues involved in the Enron scandal as an illustration, one of the major tactics deployed by Enron to manipulate its financial statements is the abuse of special purpose entities. Briefly speaking, a special purpose entity is a business entity (partnership, corporation or trust) set up by a company (its sponsor) for a special limited purpose (for example, a bank may set up a special purpose entity to purchase its receivables, hence the bank removes receivables from its balance sheet, and avoids recognizing debt incurred in the securitization). The detailed rules of US GAAP in place at that time allowed the special purpose entity not to be consolidated in the sponsor's accounts if independent third parties have a controlling and 'substantial' equity interest in the special purpose entity, where 'substantial' is defined as at least 3 percent of the special purpose entity's assets; that means, even though the sponsor and the special purpose entity are closely related, the sponsor may record gains (and losses) on transactions with the special purpose entity, and the liabilities (and assets) of the special purpose entity may not be included in the sponsor's balance sheet (it is obvious that the key to manipulation of the accounts is the special purpose entity not being consolidated). Enron sponsored hundreds of non-consolidated special purpose entities to hide debt and losses from investors. In practical operations, broadly, Enron (and its outside auditor) followed the specified accounting requirements, and ensured that the 3 percent outside-ownership rule was met so as not to consolidate the special purpose entity into Enron's statements (in spite of the fact that the person who managed the special purpose entity was not independent of Enron and often the minimum of 3 percent of equity capital that was purportedly provided by the independent outsider was, in fact, indirectly provided or guaranteed by Enron). By exploiting those non-consolidated special purpose entities, Enron reported debt as equity, generated profits by selling an asset at an inflated price to a special purpose entity, justified untrustworthy fair value estimates on the basis of a transaction with a special purpose entity, hid unprofitable investments, hedged its investments with itself, reported profits on the increase in the value of its own shares, and the like. The specific tactics of reporting debt as equity are that Enron issued its own shares to a special purpose entity, the special purpose entity paid for the shares with the proceeds of bank loans, which Enron guaranteed, and then in its consolidated balance sheet, Enron reported the shares issued (increase in equity) and the cash received (increase in assets). In reality the source of the cash was the bank loan which would have been clear if the special purpose entity had been consolidated; by not consolidating the special purpose entity, Enron was able to report as equity what was in effect debt. In the wake of the Enron scandal, the FASB tightened the rules governing the consolidation of special purpose entities, requiring them to be consolidated if the third party equity investment is less than 10 percent of total assets (instead of the previous 3 percent) or if it is probable that the sponsor will be obliged to pay out on a guarantee of the special purpose entity's debt (for more information about special purpose entity, see Benston and Hartgraves, 2002; Hartgraves and Benston, 2002; Flower, 2004b: 195-199, 216; Jackson, 2006: 162-184). Additionally, in IASB GAAP, SIC Interpretation 12 *Consolidation-Special Purpose Entities* prescribes that a special purpose entity should be consolidated when the substance of the relationship between an entity and the special purpose entity indicates that the special purpose entity is controlled by that entity.

Apart from special purpose entities, another major technique used by Enron to overstate revenue and net income was the use of fair value accounting. For instance, US GAAP requires that (long-term) energy supply contracts should be stated at fair values, however, because there is no market for that sort of contracts, managers need to estimate future cash flows and apply a discount rate to obtaining present (fair) values (namely level 3 fair value accounting, which indicates that a fair value is derived from the reporting entity's own assumptions and judgments about the future). Enron made use of those GAAP rules as follows: when Enron signed a long-term power supply contract with a company, it would project energy prices for the full term of the deal (that could be as long as ten years or twenty years), and then, based on its projections, it would calculate its total profit over the life of the contract, after discounting that total profit figure, it would book the profit immediately. To put it another way, immediately a contract had been signed, Enron recorded current gains (earnings) on the basis of its estimates of energy prices forecasted over many years. Afterwards, when changes in energy prices indicated that the contract was more valuable, additional gains resulting from revaluations to fair value were recorded (see Benston and Hartgraves, 2002; Benston, 2007 for both the above and the below instances). Another illustration of Enron's adoption of fair value accounting is that: Enron used to make its merchant investments (i.e. partnership interests and stock in untraded or thinly traded companies it started up or in which it invested) be organized as financial assets (investment funds), therefore, under US GAAP, it should revalue such assets to fair values. As was the situation for the above referred energy contracts, no market prices existed for the merchant investments, this involved Enron's managers utilizing level 3 fair value accounting. In practice, when additional earnings were required, contracts were revisited and reinterpreted if increases in their fair values could be recorded; however, recording of losses was delayed if any possibility existed that the investment might turn around. The two cases in this paragraph show that Enron booked income from increasing estimated fair values (the topic about the Enron debacle could be referred to Benston and

Hartgraves, 2002; Hartgraves and Benston, 2002; Flower, 2004b: 193-225; Jackson, 2006: 131-202; Benston, 2007).

From the foregoing instance of Enron, it could be noticed that, if there were no ethics, the principles embraced in accounting for special purpose entities would be misused (but that does not mean that the emphasis put by US GAAP on detailed rules rather than on broad principles has no responsibility for Enron's severely misleading accounts, since Enron (just) complied with the letter (but not the essence) of GAAP); if there were no ethics, the value contained in fair value measurement could not be reflected, conversely, the use of fair value could offer managers extra opportunities of deceiving investors and other users of financial statements (surely that does not imply that level 3 mark-to-model fair values have sufficient relevance and reliability to be used in the main financial statements); on the whole, if there were no ethics, preparers would not be able to correctly apply judgment, nor select appropriate principle, nor provide value which is not misleading (certainly, financial statements fraud cannot be prevented simply by ethics, instead by the functions fulfilled by the entire regulatory system, to take one example, Benston and Hartgraves (2002) hold that the SEC (together with the FASB and the AICPA) is substantially responsible for the Enron accounting debacle, because it had the responsibility and opportunity to change rules to reflect the known fact that corporations were using special purpose entities to keep liabilities off their balance sheets). It could be perceived that ethics, principle, value, and judgment are an associated and inseparable totality, which could be the intrinsic nature of accounting (and possibly the major field of accounting research). It could be observed that IASB GAAP is based on and concerned with ethics, principle, value, and judgment. As for ethics in Chinese accounting, for example, after the new ASBEs have entered into force, the Chinese accounting profession (and academics) are commonly concerned about the below matter: as mentioned in chapter 1, ASBE 12 stipulates that, in a debt restructuring event, the non-cash assets or equity interests surrendered by a debtor should be measured at fair value, and the resulting gains (or losses) should be recognized as income (this stipulation is consistent with IASB GAAP). If there were no ethics (admittedly, that does not mean only a need for ethics), that stipulation would supply management a chance of earnings management. Generally, this thesis suggests that once all of the participants in Chinese accounting have possessed the concept of accounting featured prominently by ethics, principle, value, and judgment, the convergence of Chinese accounting standards and international standards will be a natural outcome.

The second topic relates to research methods in accounting. The vast majority of literature quoted by this thesis is in relation to the study of normative accounting, which the one corresponding to is positive accounting. Watts and Zimmerman (1978, 1986) systematically expound positive accounting theory and hold that (positive accounting) theory 'is concerned with explaining accounting practice. It is designed to explain and predict which firms will and which firms will not use a particular method…, but it says nothing as to which method a firm should use' (Watts and Zimmerman, 1986: 7). They take the view that positive accounting theory is value-free study (i.e. explanation and prediction) of accounting practices and is scientific, while accounting theories concerned with prescription (i.e. normative theories) are unscientific. Another feature of the methodology of positive accounting theory is that it makes great use of statistical procedures to test hypotheses (The three chief hypotheses proposed by Watts and Zimmerman are the bonus hypothesis, the debt hypothesis and the political cost hypothesis). Sterling (1990) criticizes positive accounting theory, briefly, he asserts that financial statements should not be taken as free-floating collections of words and numerals, instead, as representations of things and events, as a result, the selection of empirical evidence is, in substance, a normative decision, and then positive accounting theory employs the choices that accountants have already made to confirm the choices accountants could make. The below footnote[1] is this writer's understanding of that issue.

This thesis is of the view that the object of accounting researches could be ethics, principle, value, and judgment (the four points could be deemed as the intrinsic nature of accounting, hence they belong to accounting), the difference between normative accounting and positive accounting is the difference of research method (rather than the difference of research object, historically, there was no that kind of difference of research method, to say, forty years ago, so it is classical), and this thesis perceives that accounting

[1] The beginning of chapter 4 raises the question about what theory is, a simple answer could be that theory is the thoughts of people who create theory. It could be considered that there are four forms in research: they prove me (in other words, I think what they think), I prove me (or to say, I think what I think), I prove them (to put it in another way, they think what I think), and they prove them (or, they think what they think). Out of the above, the research taking the form of 'I prove me' could be regarded as circularity, and the research taking the form of 'I prove them' could be perceived as plagiarism. Both normative accounting research and positive accounting research could be viewed as the research taking the form of 'they prove me', normative accounting research could draw their conclusions by analyses of other people's arguments, while positive accounting research could reach their conclusions by analyses of data provided by other people, the process of the research (from the formulation of model, to the selection of data, to the analyses of data) will be inevitably affected by researchers themselves (i.e. impossibly being value-free). There has not yet been any research taking the form of 'they prove them' arising so far, if there were, that would open up the unknown area of people's thinking (human beings may never find their way through the maze, that may be also an inherent limitation of social sciences). Moreover, the following is a proposal for further studies: As far as accounting is concerned, different accounting scholars should have many similarities in their academic thinking; as far as human society is concerned, whether literary works or academic works, whether explicitly or implicitly, could all consider that there is possibly a basic form: in terms of a specific area (e.g. accounting), an approximate triangle exists, and the people (P) at the same level share similarities (s) with each other, while the people at dissimilar levels show differences (d) from each other. If the vertex of the triangle is kept motionless, spinning the triangle (academically, involving all of academic fields) can get a sphere, and at the centre of the sphere there is an X which has never been identified by humans (it could be talked that all of the human cognition is derived from X), the distance between human and the centre is different, even if somebody can be nearer to the centre, nobody has ever reached the centre. If this conception of human society could be systematically elaborated, it could be named as the Pds theory of sociohierarchy. What is explored by this thesis is the similarities and differences in human conception of accounting, that could be regarded as neoclassical accounting. According to Pds theory, it could be assumed that there is similarity between financial accounting and management accounting, and between positive accounting and normative accounting; the importance of accounting professionalism could be perceived; it could be manifested that accounting, mathematics, and philosophy share similarities with each other. It is hoped that a book titled 'philosophical principles in accounting art (volume 1)' could be written out surrounding the foregoing, and the main content of the book embraces (1) Pds theory of sociohierarchy, (2) neoclassical accounting, (3) financial and management accounting, (4) accounting professionalism, (5) positive and normative accounting research, and (6) a general theory of accounting, mathematics and philosophy. (Here there are two points which may need explanation: the one is that the choice of 'neoclassical' is influenced by Michel Foucault, generally speaking, the surface feature of statements (about accounting) may be unimportant, but the much more important is the non-textual world (of people, institutions, and so on) connected with (and created) the statements. The other one is that the idea of 'accounting's X' is influenced by Noam Chomsky, briefly, X generates principle (besides, ethics, value, and judgment), principle generates the accruals principle, the prudence principle (and so forth), the accruals principle generates the accounting treatment that exchange differences arising on translating monetary items at rates different from those at which they were previously translated should be recognized in profit or loss in the period in which they arise (and other accounting treatments; foreign currency transaction are mentioned on pages 70 and 71).)

is people's concept of accounting, any similarity or dissimilarity in accounting should be fundamentally derived from people's different concept (or knowledge) of accounting (that relates to the people in accounting, thereby being neo), therefore this type of study taking people's concept of accounting as its research object could be named neoclassical accounting (this thesis is a preliminary study that introduces neoclassical accounting), its research method could be to explore the people behind documents by analyses of the documents. Accounting is created by people; things in relation to accounting may cover accounting standards, financial statements, accounting literature and things of that description. There is presumably a hypothesis in accounting (could be named as X hypothesis of neoclassical accounting) that anything in relation to accounting is an approximation of the accounting's X in a simple and/or specific situation. What could that X be?

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Non-Monetary Transactions (issued in 1999 and revised in 2001)
Leases (issued in 2001)
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Basic Standard (the 2006 Basic Standard)
ASBE 1 Inventories
ASBE 2 Long-term Equity Investments
ASBE 3 Investment Property
ASBE 4 Fixed Assets
ASBE 5 Biological Assets
ASBE 6 Intangible Assets
ASBE 7 Exchange of Non-monetary Assets
ASBE 8 Impairment of Assets
ASBE 11 Share-based Payment
ASBE 12 Debt Restructuring
ASBE 13 Contingencies
ASBE 15 Construction Contracts
ASBE 16 Government Grants
ASBE 18 Income Taxes
ASBE 19 Foreign Currency Translation
ASBE 20 Business Combinations
ASBE 21 Leases
ASBE 22 Recognition and Measurement of Financial Instruments
ASBE 23 Transfer of Financial Assets
ASBE 24 Hedging
ASBE 27 Extraction of Petroleum and Natural Gas
ASBE 30 Presentation of Financial Statements
ASBE 31 Cash Flow Statements
ASBE 35 Segment Reporting
ASBE 36 Related Party Disclosures
ASBE 37 Presentation of Financial Instruments

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Framework for the Preparation and Presentation of Financial Statements (the IASB Framework)
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IAS 2 Inventories
IAS 7 Cash Flow Statements
IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors
IAS 11 Construction Contracts
IAS 12 Income Taxes
IAS 14 Segment Reporting (superseded and withdrawn)
IAS 16 Property, Plant and Equipment
IAS 17 Leases
IAS 19 Employee Benefits
IAS 20 Accounting for Government Grants and Disclosure of Government Assistance
IAS 21 The Effects of Changes in Foreign Exchange Rates
IAS 22 Business Combinations (superseded and withdrawn)
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SFAC 6 Elements of Financial Statements
SFAS 2 Accounting for Research and Development Costs
SFAS 13 Accounting for Leases
SFAS 15 Accounting by Debtors and Creditors for Troubled Debt Restructurings
SFAS 19 Financial Accounting and Reporting by Oil and Gas Producing Companies
SFAS 25 Suspension of Certain Accounting Requirements for Oil and Gas Producing Companies: an amendment of SFAS No. 19
SFAS 69 Disclosures about Oil and Gas Producing Activities
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SFAS 115 Accounting for Certain Investments in Debt and Equity Securities
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ARB 43 Chapter 4 Inventory Pricing
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SSAP 13 Accounting for Research and Development
SSAP 19 Accounting for Investment Properties
SSAP 20 Foreign Currency Transaction
FRS 18 Accounting Policies