


Thinking Globally
Setting Standards Locally



The formal announcement in February 2006 of China's new Accounting Standards for Business Enterprises was warmly welcomed by the Hong Kong and international accounting professions. The new standards cover almost everything that is authorised by the International Financial Reporting Standards (IFRS) and are set to become mandatory for all listed Chinese enterprises from 1 January 2007. *Australian CPA Network* asked Stephen Taylor, partner, Deloitte Touche Tohmatsu, which has worked as a consultant to China's Ministry of Finance since 1992, to highlight some of the differences between the new Chinese standards and IFRS, and to comment on their efficacy and wider implications

Q. What are the new standards and which companies will they affect?

Stephen Taylor: The Accounting Standards for Business Enterprises are to be implemented in phases. Phase one is all listed entities from 1 January 2007. That means the PRC-listed entities, which are overseen by the China Securities Regulatory Commission (CSRC), the securities regulator. In understanding the implications of the timing of these standards it is important to consider any additional requirements the CSRC, in its position of regulator, may require for December 2006 year ends. In other jurisdictions where new standards have been implemented listed companies have been required to detail the implication on their accounts of these new standards prior to their implementation. As for many A share companies the changes brought about by these new standards could be significant and it will be interesting to see what the CSRC's requirements or transitional reliefs might be.

The accounting system for business enterprises was put in place some years ago; it is China's foundation standard and it is embedded in the law. The existing guidelines spring from this accounting framework and the Ministry of Finance (MoF) has the authority under the law to promulgate specific Chinese standards. When China started opening its doors in the 1980s it realised it needed an accounting framework in place because it was moving towards more of a profit-oriented economy. Its old accounting rules were geared to the command economy, and they didn't give relevant financial information on which to base decisions about the efficient allocation of resources. In the 1980s China brought out some accounting rules and later on standards. In 1992, the World Bank tried to encourage a more comprehensive accounting structure. Deloitte was employed in China to advise the MoF in drafting accounting standards to meet the needs of its growing market-driven economy. This exercise resulted in 30 exposure drafts which proposed accounting standards many of which were similar to the ones the International Accounting Standards Board (IASB) had in place at the time. Of the *Cont'd over*

30 exposure drafts, 16 standards eventually emerged released on an 'as needs' basis.

Since 2000, China has been viewing the developments at the IASB and looking at developing a much more comprehensive framework with the view to convergence and to contribute to the IASB's objective of a single set of global standards. It has now issued a comprehensive system that is similar to the IFRS but some differences remain. An example of these differences is the elimination of choice; when China was developing its standards it tried not to build in choice. So in comparison to IFRS, which inherited a number of choices from its previous standards, China has tended to eliminate certain options and in doing so may be highlighting eliminations that may be the way the IASB goes in future.

An early example of this would be borrowing costs where the current IFRS allows you to either capitalise or expense. Where the relevant criteria are met the Chinese Standard only allows capitalisation. Subsequently the IASB has released a new exposure draft that also supports the 'capitalise only' option. Another example would be for joint ventures. The IFRS currently allows both proportional consolidation and equity accounting. We know one of them is going to be eliminated. The Chinese standard eliminates proportional consolidation and therefore only allows equity accounting. From following the debate at the IASB meetings it would not be a surprise to see the IFRS follow the same route.

Q. Do you truly believe that China will take onboard international standards?

ST: Yes. We're talking about roughly 1,500 listed companies to start with. These are major corporations. A lot already have H shares or B shares and these already report under IFRS. One of the issues is that the H shares and B shares are in practice audited by the Big 4 so there is some knowledge base there. But only about 12 percent of the remaining listed companies are audited by the Big 4. A majority of them have local CPAs and no access to the same kind of support and assistance to help them in their implementation of the new standards. Having said that, one of the things that may be a saving grace for many is the fact they are not very complicated companies. For a genuine nuts and bolts manufacturer, for example, the accounting standards won't affect them too much - they won't have share options or financial instruments or complicated revenue transactions.

However, there is an issue over whether there are enough qualified CPAs in place in China to deal with the implementation. We are talking about a minimum of 1,000 major listed companies and many are enormous. Some of them have hundreds if not thousands of subsidiaries. One good thing is that their bookkeeping has been good,

particularly those that were state-owned industries. The MoF also understands the need for support and is planning to provide two to three weeks training for listed entities and CPAs. It is also in the process of issuing implementation guidelines, which are currently under review and are intended to come out before September 2006.

Q. How will the lack of competent people affect the implementation of the standards?

ST: It will limit the fact that the Big 4 can help. We can help in terms of training and support materials and trying to ensure that accountants are educated in the new standards. But finding experienced people is going to be a problem. It's not helped by the fact that elsewhere in the world there is a shortage of these qualified individuals with many countries going through a similar transition in accounting standards. Nor is it easy for us to call on our other offices and ask for people because there is the additional problem of language in China. The other thing is that all these listed companies in China will also be wanting to employ qualified and experienced people in-house, and the Big 4 is where these people may currently be working. So as they come up through the grade and move into more senior positions they become very valuable assets for anyone else in China because they have been through comprehensive training and have real life experience with these new standards. Are we going to help China? Yes, we will be educating their CFOs and finance heads of the future.

Q. What is set to happen after the first phase implementation in listed companies?

ST: We will probably see some of the state-owned industries start to implement the new standards. They may be under pressure to do this or they may want to do it because they plan to seek a listing in Hong Kong or overseas. But I suspect there will be a move from some of the state-owned industries to move earlier rather than wait until they are actually required to move. The bigger issue will be whether Chinese companies will be allowed to list on overseas exchanges using PRC GAAP. This is being discussed now with various regulators and exchanges worldwide. In the European Union, for example, they have already said they will allow Japanese GAAP for Japanese companies listing.

Q. But isn't the whole idea of convergence to have one set of standards?

ST: Yes. And that's why countries, particularly their stock exchanges, which were the drivers of getting a standard set of accounts worldwide, have to be conscious of that fact because what we're seeing is political pressure on them to accept the fact that some of these countries are so close to IFRS. This debate is yet to be had. Obviously, one of the cornerstones of China moving to IFRS and convergence is that it would like to see its standards accepted as a world



class set of standards. It is still looking to converge but it is also saying that it believes that convergence is the move to the highest quality standards and some of its practices are things that the IASB should consider or adopt.

Q. Why can't you have one set of IFRS standards with exceptions for specific circumstances in each country?

ST: Ideally, that's where we should be but it's mainly the lack of sovereignty that is the issue. In China the standards are laws. So you would be allowing a body of people sitting in London to dictate their laws. Hong Kong won't do it, neither will the European Union. Even in the European Union if an IFRS standard is issued by the IASB it has to be endorsed by the European Union for use in Europe because it's a legal issue. What we will probably see more of in China's case is a reconciliation requirement. In other words, it will be alright to use this Chinese standard but please reconcile and show us the potential impact of these minor differences.

Q. What should accountants based in China be doing now in preparation for the implementation of the standards?

ST: One of the things they should be doing is getting up to speed. At the moment there is not a lot of training material available on PRC GAAP because it's only just come out. We will issue a GAAP differences book that will go through each standard and look at the differences. For most of the standards there are no fundamental differences with IFRS and even where there are differences the rest of the standard is basically the same. If you want to start now the best thing to do is to start learning IFRS. Deloitte is in the process of translating into Chinese its e-learning for IFRS and we hope to release the first five or six modules to coincide with the guidance release, which is probably 1 September. That will be a good way for people in China to get up to speed with the basic awareness of what the accounting standards are.

Q. Going back to the second phase, what other entities will be required to implement the new system?

ST: At some stage they will probably widen the requirement to cover, for example, the foreign joint ventures. In fact some of the foreign joint ventures may choose to early adopt because they won't want to be adopting two sets of standards. They already report to their parent companies or joint venture partners in IFRS or equivalent Hong Kong GAAP. So they may early adopt because they're allowed to and then they will only have to produce one set of accounts. On the other hand, I don't think they will push the standards down to the small and medium-sized enterprises (SMEs) yet; they already have an Accounting System for Small Business Enterprises so I think they will wait and see what the IFRS SME standards will say.

By IMC Staff Writers



Where can you find the most stars in Australia?

University of South Australia (UniSA) has been awarded 35 stars in total, and ranked No.1 by The Good University Guide (MBA & Executive Courses) 2006. It has received the most stars among all Australian MBAs. UniSA Division of Business programs are **EQUIS** accredited.

DBA

(Reg. No. 210125)
HK 13th Intake
(2 ½ years)

Doctor of Business Administration

- UniSA division of business programs are EQUIS accredited
- Successful track record of over 250 PhD/DBA graduates in the region to date
- Currently successful track record of 92 PhD/DBA graduates in Hong Kong
- Unique program suitable for academics, business consultants and senior management practitioners
- CEF Reimbursement available for selected courses



MBA

(Reg. No. 210002)
HK 44th Intake
(1 ½ years)

Master of Business Administration

- Well Established & Proven Track Record - 13 Years in Hong Kong with over 2,000 graduates in Hong Kong to-date
- Taught by University academics with extensive practical knowledge offering global business & management perspectives
- Accelerated completion within 1 ½ Years
- 4 subjects may be exempted for CPA / ACCA / HKICPA full members*
- CEF Reimbursement available for selected courses



CPA (Australia)

CPA (Australia)

* Exemptions are subject to university approval on a case-by-case basis.

☎ 2836 0332 or 🌐 www.apmi.com.hk



Asia Pacific Management Institute
6/F, Luk Kwok Centre, 72 Gloucester Road, Wanchai, Hong Kong

It is a matter of discretion for individual employers to recognize any qualification to which these courses may lead.

"個別僱主可酌情決定是否承認本課程可令學員獲取的任何資格"