

University of Economics in Prague

Faculty of Finance and Accounting

Finance and Accounting



MASTER THESIS

**IFRS Adoption and Its Influence on Capital Market  
in Transition Countries—The Case of China**

Author: Bc. Ming Xu

Supervisor: doc. Ing. David Procházka, Ph.D.

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## **Declaration of Authorship**

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## **Abstract**

Accounting is considered as a general economy and finance language which plays a significant role in the business society. The capital market is a key part of economy which cannot get through without the development of accounting. In recent years, Accounting harmonization gains more and more awareness from some studies of accounting practice and theory which aims to increase the attractiveness of capital markets by reporting high-quality financial statements in the way of reduced financing costs.

Based on the international standards of financial accounting, this essay focuses on observing the process of the Chinese accounting harmonization. Then, further analysis will be conducted on the comparability index between those two kinds of standards on the basis of capital market and return on net assets of public companies. This analysis is going to investigate the items of accounting which tend to significantly impact the features of the industry.

**JEL Classification:** M41, M49, G3

**Keywords:** Accounting Standards for Business Enterprises, International Financial Reporting Standards, Capital market, Transition economy, China

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# 1. Introduction

Accounting is considered as a general economy and finance language which plays a significant role in the business society. Nowadays, with the development of world economic integration, the establishment of unified and high-quality accounting standards on a global scale has become an inevitable choice for the world's major economies. Convergence is a great direction and trend, accounting harmonization gains more and more awareness from accounting practice and theory. Lots of countries and organizations, for example, United States, Japan and European Union, are trying to move up the process of the convergence of international accounting standards actively in order to compete for global leadership and capital markets.

The objective of this thesis is to investigate the adoption of International Financial Reporting Standards (IFRSs) and its influence on capital market. When talking about international convergence of accounting standards, adoption of IFRS is mentioned a lot. The goal of setting IFRSs is to make the financial market more transparent, accountable, and efficient, therefore, firms from different countries can understand each other and compare their financial information. The capital market is an important part of economy which cannot get through without the development of accounting. Once different kinds of accounting standards get unified, their capital markets will be more attractive for various stakeholders by reporting high-quality financial statements in the way of

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reduced financing costs and increasing liquidity of capital.

This thesis is divided into the theoretical and practical part. The content of theoretical part includes four parts. To start with the topic of accounting harmonization, the first part will introduce IFRSs and its function, as well as how IFRSs are developed by IASB. The reasons caused accounting difference will be discussed in the second part from the economic, politic and legal angle. Based on the information included in previous sectors, the importance of accounting harmonization of IFRSs can be further discussed in the third part. Therefore, the fourth part will explore the approaches of applying IFRSs and its impacts on capital markets. The practical part will focus on comparing the similarities and differences of IFRSs and China's Accounting Standards for Business Enterprises (ASBEs) to find out the possibility to deepen the coordination between China's Accounting Standards Committee (CASEs) and IASB for further convergence by analyzing the background, specific standards like impairment of assets, fair value measurement, employee benefits and the disclosures of the relevant parties. In order to find out whether the harmonized ASBEs with adoption of IFRSs have positive effect on China's capital market, this thesis will choose the Chinese companies both listed in mainland China where applies ABSEs and Hong Kong where applies IFRSs as study subjects. The analysis will focus on the net profit comparison of the same company under two different criteria with the method of comparability index and return on net assets and try to answer the question that will adoption of IFRSs eliminate the effect of comparability index and enhance the effect of return on net assets.



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## 2. Literature review

In the following section, the rationale of this thesis will be presented and the relevant consequences of the previous researches will be discussed.

When talking about accounting hominization, we are mainly talking about adoption of IFRSs, which is quite complex and may have resulted from those compulsory regulations of accounting, equity owners' requests, initiative of the management and the demand for comparative information. According to Nobes and Parker (2008), “‘Harmonization’ is a process of increasing the compatibility of accounting practices by setting bounds to their degree of variation. ‘Harmony’ is the state where compatibility has been achieved. ‘Standardization’ appears to imply working towards a more rigid and narrow set of rules”. (Christopher & Robert, 2008) It implies that different accounting standards on a global scale can be a good match.

The reasons cause international accounting difference include languages, tax systems, legal systems, economic levels, culture difference and financing sources. Nobes (2011) presents theory-based reasons for the variation of accounting practices and regulations from country to country which is the lack of enough endeavors to strive for internationally harmonized and standardized practices of accounting. Users of accounting information can be divided into two parts: inside users and outside users. Accounting systems are different according to the different size of capital markets and

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different roles of information users.

Hence, there is an expectation and an unavoidable trend of the internationally different financial reporting. The high flexibility and various options of the IFRSs play an important role in enterprises' adoption to it. The way of business operations varies from country to country, specifically in their core industries, contract types, etc., which makes their options extremely necessary. According to Beke (2010), who explained how the globally standardized accounting system facilitates decision-making in business and impacts the environment of economy, the international accounting system of unification and harmonization will accelerate the accumulation of data and analysis, also probably accompanied with the new indicator integration from the management of businesses in specific nations.

Generally, adoption of IFRSs have a positive influence on both the capital market and firms which shows in unifying business transactions, improving transparency, enhancing comparability, enhancing market efficiency, and global integration of local companies. However, it doesn't mean that every country or region should fully adopt IFRSs without hesitation. Through the studies on these countries and regions which are applying IFRSs, three approaches have been used which are direct adoption approach, convergence approach, and Endorsement approach. Besides, the fourth one condorsement approach were introduced according to United States Security Exchange Commission (SEC)'s *Work Plan for the Consideration of Incorporating International*

In China, there are also some studies on harmonization of ASBEs with IFRSs. Chinese Ministry of Finance released *the Roadmap for Continuing Convergence of Chinese Accounting Standards for Business Enterprises with International Financial Reporting Standards* in April 2010. The roadmap points out the advantages of adoption IFRSs, which include improving transparency, unifying business transactions, enhancing comparability, enhancing market efficiency and global integration of local companies. On the other hand, Yang, Lu, and Xu (2011) explored four kinds of possible approach that China may apply when adoption IFRSs, they are direct adoption approach, convergence approach, endorsement approach, and condorsement approach (Yang, Lu, & Xu, 2011) .

There are several studies analyzing the differences between IFRSs and ASBEs about their framework and specific accounting standards to demonstrate the feasibility for full adoption of IFRSs in China. Liu (2007) had examined that ASBEs emphasizes that major economic businesses and accounting elements should be recognized, measured and reported, based on the requirements of the accounting records. However, accounting records do not belong to IFRSs. IFRSs mainly regulate accounting recognition, measurement, and reporting. Other specific differences appear in related party disclosures, impairment of assets, business combinations under common control, fair value measurement, employee benefits, financial reporting in hyperinflationary

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economies and investment property. Considering the situation in China nowadays, the specification for accounting records is still needed for the reason that it can make ASBEs more operational and facilitate the implementation of a comprehensive and accurate standard system (Yuting, 2007).

Moreover, Grey (1980) provides theoretical explanations for comparability index. In his research, a "Conservatism" Index was introduced for comparison between different accounting standards which refers to an index that expresses the adjusted profits that are linked to disclosed profits and presents an unbiased indicator for the corporate measurement of the enterprises in various nations (Gray, 1980). The conservatism index has also been known as the "index of comparability" in recent years and been applied to compare with the accounting data published for the same enterprise under various regimes of accounting (Haverty, 2006).

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### **3. Accounting harmonization of IFRSs**

Along with the global economic integration, cross-border trades and import and export trades happen more frequently. A popular accounting topic about how different accounting standards work together at the same time gains more and more awareness from some studies of accounting practice and theory which aims to show the world that different accounting standards can be a good match. Therefore, considerable attention has been paid to IFRSs adoption all over the world.

#### **3.1 IFRSs and IFRS Foundation**

The development of international accounting standards began with the establishment of International Accounting Standards Committee (IASC) in the year 1973. The IASC is mainly initiated by a consensus reached by a group of professional accounting institutions from the US, the UK, Netherlands, Mexico, Japan, Germany, France, Canada, and Australia, aiming at providing countries with substantial and high-quality accounting standards (Deloitte, 2017). Till now, most of the countries in the world are presented in this organization, China also joined this organization in 1998 as sponsoring members. IASC is more like a structure than the real committee composed of a group of people. It is a process for setting International Accounting Standards from 1973 when it formed to 2000 when it was comprehensively reorganized (Deloitte, 2017).

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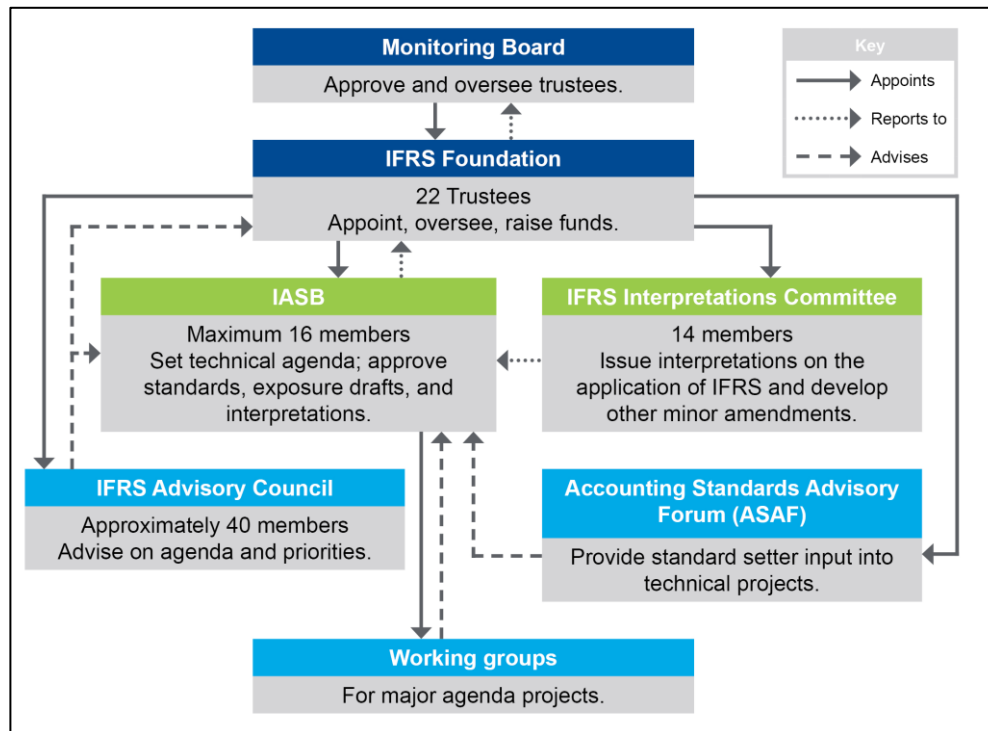
The establishment of the new International Accounting Standards Board (IASB) was completed in the April of the year 2001, and it has been established to develop the IFRSs and promote the application of the standard. The board comprises of a bunch of professionals with independence and expertise from different countries, who have abundant experience in accounting education, financial reports application, auditing and accounting standard setting. IASB decided to continue using and revising the previous international accounting standards. After that, the new guidelines on the development of IFRSs, including "financial reports and conceptual framework", "international accounting standards" and "Standing Interpretations Committee interpretations" issued by the IASC successively from 1973 to 2001. "Interpretations Committee interpretations" as the official has explained before, together with other technical summaries of the revised and official documents promulgated by the IASB have been put into use since 2001.

The purpose of setting IFRSs by IASB is to allow firms from different countries to understand each other and compare their financial information and interpretations. The goal is to make the financial market more transparent, accountable and efficient through the development of IFRSs. Nowadays, IFRSs have extensively been adopted as the worldwide standards of accounting, with more than 120 countries applying them substantially and around 90 of these counties need full convergence to them. Therefore, the need for the assessment of the real impacts on capital markets is obvious. (IFRS, 2017)

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Based on the data in figure 1, the structure of IFRSs contains three parts of governance, technical and advisory. In governance part, IFRS Foundation has the duties to supervise IASB's strategy, structure and work, as well as raising funds since it is not a profitable organization. Monitoring board takes the responsibility to supervise the twenty-two Foundation Trustees through participating into the nomination of Trustees and the approval of Trustees appointment. And the Trustees needs to govern and monitor the practices of IFRS Foundation in, such as operational procedure amendment, yearly budget approval, funding, etc. The technical part is made up of IASB, IFRS Interpretations Committee and working groups whose function is to establishing IFRSs and developing interpretations. The advisory part has included Accounting Standards Advisory Forum (ASAF), IFRS Advisory Council whose functions are shown in figure 1.

Figure 1: structure of IFRS Foundation



source: Deloitte

In the beginning, the IFRSs only determined the broad definition which is not implemented to address specific business methods. Until 2002, a number of alternative treatment methods were gradually released. These guidelines are the foundation of principle. What's more, IFRSs specially set general purpose and key issues of financial reporting, measurement, recognition and disclosure standards, and set up specific rules for certain industries.

For multinational enterprises in China and those who have the investment in China. IFRSs and Accounting Standard for Business Enterprises (ASBEs) are two important



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criteria of a wide range of applications. Coordination between these two criteria has become a popular and inevitable topic of accounting theory and accounting practice. If the companies can understand the similarities and differences between IFRSs and ASBEs with international norms more clearly, there is no doubt that it will be more conducive for them to grasp the opportunities in the world competition. It will also be more conducive to report high-quality financial statements and reduce financing costs. In addition, understanding these two criteria is important for continuous improvement of accounting system no matter in China or the world. The gradual convergence of IFRSs and ASBEs can be demonstrated that they match well instead of contradiction.

## **3.2 Main reasons**

### **3.2.1 Differences in legal system**

Legal systems restrict accounting standards and accounting systems. The legal system can be roughly divided into two categories: code law and common law. Typical countries that applies code law system are Germany, France, and Japan. In these countries, accounting practices and financial reporting regulations are formulated by the government which are usually recognized as part of tax law, commercial law, etc. Whether the financial reports can fairly and accurately reflect the performance and results of a company are placed in a secondary position. Countries such as United States, United Kingdom, Canada and Hong Kong apply common law system. The main feature

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of their accounting system is that accounting standards are formulated by independent private institutions. Accounting standards are separate from tax law and commercial law which emphasize the accurate and fair reflection of companies' financial position and operating results.

### **3.2.2 Differences in economic levels**

The development level of accounting standards largely depends on that of the economy. Developed countries usually have experienced accounting practice, rigorous accounting standards, and sophisticated accounting systems because of their complex economic relationships.

### **3.2.3 Differences in culture**

Different cultures of different countries are considered to significantly impact the behavior of disclosure and reporting of finance (E.g. collectivism vs individualism, adventurism vs risk aversion, diversity vs uniformity, confidentiality vs disclosure, etc.)

Public culture influences social values and has a significant impact on people's ways of thinking and behavior. In a democratic nation, people are more likely to have the strong awareness of individuals. Respect for professional judgments is often made by more developed professional accounting organizations. In a comparatively absolutist nation, accounting standards are possible to be used by the person in power.

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### 3.2.4 Differences in financing sources

Different international accounting standards may have resulted from plenty of causes. According to Nobes (2011), those potential causes can be concluded into one major reason: different methods of corporate financing, which presents both the internal and external dimensions. Internal users are those investors that hold a debt-related or equity-related relationship with the corporation in the long run, such as family members, banks (as major lenders or shareholders) and the government. These internal users probably are entitled to the appointment of the member of the board, or to be accessible to the corporate information. External users, by comparison, are the millions of shareholders whose shares take little account of public companies since they don't have the privilege of company information for the worry of violating insider-dealing laws in the relevant state. Included in this group are large shareholders like the American or British pension funds. (Nobes, 2011)

Table 1: Classification and examples of the financing systems

<b>System I</b>	credit	inside users	associated with several continental European countries in the 19th and 20th centuries;
<b>System II</b>	credit	outside users	might be rare, but there is a vast amount of listed debt on the New York Stock Exchange;
<b>System III</b>	equity	inside users	elements of which are seen in Japan;
<b>System IV</b>	equity	outside users	the full-blown capitalism of New York and London ; China has moved towards System IV but the State (an inside user) still holds much equity.

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<b>dominant investors</b>	<b>strong credit</b>	<b>strong equity</b>
inside users	I	III
outside users	II	IV

Source: (Nobes, 2011)

As shown above, accounting systems are different according to the different size of capital markets and different roles of information users. There may be more than one system in the same country. For instance, large corporations in the country may adopt System IV, while small ones may adopt System I.

### **3.3 Advantages of adopting IFRSs**

Accounting principles like accounting rules and guidelines are engaged by accountants, but why not different countries use the same accounting criteria? I think there are many reasons. For example, Generally Accepted Accounting Principles in the United States (US GAAP) are adopted primarily by American companies or Wall Street listed companies. IFRS are mainly applied in European countries, also in Hong Kong, Russia, Australia and other countries. However, international standards cannot be suitable for the condition of all countries, so it is necessary to implement convergence and integration work for accounting harmonization. IFRSs refer to the common rules of reporting and accounting which present the commonly accepted transaction reporting and recording, and the appropriate disclosure in the financial statements of a

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corporation. Since the cross-nationally application of IFRS has increased a lot, they have become crucially important to the international financial reporting. The establishment and application of IFRSs allow the government, organizations and the investors to make comparisons with differently-sourcing financial statements more easily. The advantages of adopting IFRSs are as follows:

### **3.3.1 Unifying business transactions**

Compared with domestic accounting standards, IFRSs try to consider each enterprise around the world on the same dimension when it refers to how to disclosure financial statements, then local enterprises are possible to evaluate themselves by making comparisons with competitors in other countries. what's more, adopting IFRS can let transnational corporations and their subsidiaries consolidate and prepare annual reports in the same language which is understandable for everyone. Adopting unified reporting and accounting standards can avoid different financial statement results.

### **3.3.2 Improving transparency**

Transnational corporations and their subsidiaries can harmonize their operation, reporting, auditing and training standards in regional markets under IFRSs. The adoption of commonly used standards will allow corporations to monitor their subsidiaries' operations and therefore improving transparency. No matter the

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corporation is domestic or global, their subsidiaries can apply similar standards for reporting and accounting to provide financial information of consistency.

### **3.3.3 Enhancing comparability**

it is quite challenging to analyze and present financial statements under different accounting standards. IFRSs can enhance comparability by allowing corporations from various nations to adopt similar standards for accounting. After becoming more transparent, the commonly used standards will make international trades easier by decreasing capital cost and increasing liquidity. It is also possible to avoid information asymmetry and make it easier for cross-border investors to know how is their company performing, make full use of the disclosed information then do better choices.

### **3.3.4 Enhancing market efficiency**

Using the same accounting standards will help companies save capital in the long turn as the way of shortening the time of preparing financial statements and the costs of reporting under different systems. What's more, once investors get the accurate and timely financial information to make better investment decisions, it will bring up the performance and efficiency of the whole capital market. Applying various accounting standards is compulsory for lots of corporations if the local supervision departments don't recognize the advantages of unified accounting standards which will lead to high

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costs of preparing financial reports and unavoidable risks of reporting errors. As a result, market efficiency can never get enhanced.

### **3.3.5 Global integration of local companies**

Adopting the same standards makes it clear to see the difference between local companies and their competitors in other countries which will enable them to compare their financial statements and learn from each other to achieve performance improvement. It will also help increase the chances of mergers and acquisitions for such companies in the related field. With no application of similar standards, the corporate evaluation shall cost a lot and cross-national acquisitions mergers will be discouraged.

In view of the above advantages of the adoption of IFRSs, each individual, company, and government around the world should consider adopting it for financial reporting. However, it doesn't imply that we should ignore other standards. Diversified accounting standards, for example, US GAAP and IFRSs, have an effect on making accounting standards more credible and efficient in the competitive market. As other standards become available, IFRSs will continue to be improved and deal with the public's worry about its efficacy. From the above, the advantages of adopting IFRSs have shown more opportunities than risks. Therefore, no matter what the business is, everyone has a relationship with the standards and shall familiarize themselves with them.

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### **3.4 Assumption of the consequence of accounting harmonization**

Despite of different accounting standards, every country or region has the same requirement to ask its accounting participators to provide timely and effective accounting information to the public for helping them make right decisions. With the number of cross - border investment and multinational companies increasing, the process of international harmonization has been greatly accelerated. Accounting harmonization makes it easier for management of multinational companies which represents the general trend. Harmonization of IFRSs is undoubtedly an inevitable requirement of economic globalization. Till now, one may have the question that are IFRSs the only choice for accounting harmonization?

Because of the different economic and social systems among the world, it brings the unavoidable cost of translating and understanding accounting information additionally. The convergence of IFRSs is still a period of seeking common points while reserving difference. Each country's accounting system has its own distinct characteristics. The economic basis determines superstructure, accounting belongs to the category of the superstructure and is affected by social and market types. It is also doubtful that will be accounting harmonization be conducted successfully in every country or region? And if it is conducted successfully, what kind of approach will be implemented?



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## **3.5 Consequences and approaches to accounting harmonization**

### **3.5.1 Inevitability of IFRSs**

Compared with IFRSs, Generally Accepted Accounting Principles in United States (US GAAP) is also a widely used accounting standards. Due to the Enron accounting scandal in the USA, IFRSs have gradually been recognized and valued by more and more countries and companies. As a result, United States changed its attitude toward international accounting organizations after Enron accounting scandal and actively participated in the construction of the international accounting theory framework. At the same time, many developing countries are learning the advanced features from IFRSs to develop their own national accounting theory. On the other hand, in order to attract more investments from developed countries, developing countries adopt generally accepted accounting standards consciously, which greatly reduces foreign investor's management barriers to their multinational subsidiaries and increase transparency and effectiveness of their accounting information.

For most of the transition countries, during the last 10 years, they have gone through the challenging situation where they have been transformed into a market-oriented economy from the original centrally-planned economy. If some transition countries follow the accounting standards directly designed by those countries with the highly

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mature market economy, although they can benefit from the convenience of free trade, they have to take high costs for translating and understanding foreign account standards and face the problem raised from mismatches and market chaos in the beginning. At the same time, we can see that accounting theory cannot cover all economic businesses. It is impossible for any accounting theory in certain regions for a given period of time to be universal. It must be different according to different circumstances.

In recent years, the application range of IFRSs has been continuously expanded around the world. More than 100 nations or regions have adopted or converged with IFRS directly. European Union, Australia, Hong Kong, and other regions have been operating IFRS since 2005. A few years later, the international convergence of accounting standards has attracted more attention: Japan, South Korea, India, Canada, etc. have made the announcement about the plan of applying international standards or the convergence with them. The United States has also issued guidelines to step up its convergence with international standards in November 2008. Since the financial crisis, although the accounting problems caused by fair value have become the focus of the accounting profession, the determination of the Securities and Exchange Commission (SEC) to converge with international financial reporting standards remains unwavering.

Table 2 is the list of IASB Board membership. In order to process accounting harmonization all over the world, diversified nationalities of the membership who are practically experienced are required when it comes to financial reports application,

auditing, accounting standards establishment, and accounting education. Among the current 14 IASB members, there have been 4 European members, 4 Asian members, 4 American members, 1 African member and one from an area as appoint, aiming at the maintenance of the overall geographically balanced state.

Table 2: IASB Board membership

Board member	Term began	Term ends *	Region
<b>Chairs</b>			
<a href="#">Hans Hoogervorst</a> ( <i>Chair</i> )	July 2011	June 2021	'At large'
<a href="#">Sue Lloyd</a> ( <i>Vice-Chair</i> )	January 2014	December 2018 *	'At large'
<b>Members</b>			
<a href="#">Nick Anderson</a>	September 2017	August 2022*	Europe
<a href="#">Martin Edelmann</a>	July 2012	June 2022	Europe
<a href="#">Françoise Flores</a>	January 2017	December 2021 *	Europe
<a href="#">Amaro Luiz de Oliveira Gomes</a>	July 2009	June 2019	Americas
<a href="#">Jianqiao Lu</a>	August 2017	July 2022*	Asia-Oceania
<a href="#">Gary Kabureck</a>	April 2013	June 2022	Americas
<a href="#">Takatsugu (Tak) Ochi</a>	July 2011	June 2019	Asia-Oceania
<a href="#">Darrel Scott</a>	October 2010	June 2020	Africa
<a href="#">Tom Scott</a>	April 2017	March 2022*	Americas
<a href="#">Chungwoo Suh</a>	July 2012	June 2022	Asia-Oceania
<a href="#">Ann Tarca</a>	July 2017	June 2022*	Asia-Oceania
<a href="#">Mary Tokar</a>	January 2013	June 2022	Americas

Source: Deloitte

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There has been a global consensus on converging with international accounting standards and the corresponding actions. Nearly 120 countries and regions in the world have requested or permitted the adoption of IFRSs or convergence with IFRSs. IFRSs have strong impacts on the economic resource allocation worldwide and directly cause the wealth transformation in the global society. Through the studies on these countries and regions, it has been found that the strategies for applying IFRSs are mainly divided into three categories: direct adoption approach, convergence approach, and Endorsement approach. Besides, the US SEC introduced the fourth one endorsement approach in “*Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers*” published in May 2011. Comparing and analyzing the characteristics, impacts, and operating environments of these four approaches will help us scientifically explore the international convergence of IFRSs.

### **3.5.2 Direct adoption approach**

Under the direct adoption approach, the accounting standards of a country or region will fully adopt IFRSs, and the country or region will not retain the accounting standards setting right. In other words, the country or region does not need to perform any approval or revision procedures in the adoption of IFRSs. At present, only a few countries or regions in the world adopt the model of accounting standards that are directly adopted by IFRSs, for example, Australia.

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### **3.5.3 Convergence approach**

Under the convergence approach, the standard setting boards of these countries or regions do not directly incorporate the IFRSs issued by IASB into their accounting standards system. However, they keep the determination right to formulate local accounting standards. Instead of completely complying with IFRS, the countries or regions adopting the convergence model will be consistent with IFRS only in the approaches and foundations of accounting and keep certain national features. For example, India typically conforms to this model.

Based on the Companies Act of 1956, the Indian central government was responsible for the formulation and promulgation of the accounting standards in India. In the first month of 2011, the Indian Institute of Certified Public Accountants, which takes the responsibility to formulate the accounting standards in India, has reformulated its own accounting standards on the basis of IFRSs. While achieving convergence with IFRSs, it also takes into account the domestic environment of policy, law, and economy. Indian accounting standards have been appropriately modified based on India's particular national conditions. For example, setting the transition date of the standard to the current period, introducing additional disclosure requirements, omitting certain options or optional accounting treatments, and retaining the term like balance sheet and income statement.

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### **3.5.4 Endorsement approach**

Under the Endorsement approach, a country or region will decide on the adoption of IFRSs after their statutory authority enforce accreditation procedure that aims at the stakeholder protection. When accrediting IFRSs, the statutory authorities of these countries or regions may revise IFRSs. In other words, the statutory authorities apply individualized IFRSs to set their local standards.

The European Union and Australia are typical representatives of this model. Before the European Union adopts IFRSs which is promulgated by IASB, they must get the approval of European Parliament and the European Commission no matter they adopt IFRSs directly or adopt it after modification. In Australia, the law confers the Australian Financial Reporting Council the responsibility to supervise the establishment of Australian accounting standards and auditing standards, and give direct guidance for the Australian Accounting Standards Board in introducing IFRSs. The Australian Accounting Standards System not only include the framework of the IFRSs, but also adds specific content for non-profit organizations based on the specific requirements of the Australian legal environment.

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### 3.5.5 Condorsement approach

Under the condorsement approach, a country or region will promote the convergence of domestic accounting standards and IFRSs, while retaining the national accounting standard - setting boards and their responsibility to formulate their own national accounting standards. Each standard of IFRSs shall be accredited in accordance with the actual conditions of the country or region, then further guidelines, explanations or other disclosure requirements shall be issued.

On May 26, 2011, U.S. SEC issued a draft “*Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers*”<sup>1</sup> where the brand-new model “condorsement” was introduced to the public for the first time. In this work plan, SEC stressed that the goal of “convergence” is to integrate the IFRS into the financial reporting system of the USA instead of using the IFRS to replace the US GAAP, that is, not U.S. issuer adopts IFRS, but the U.S. financial statements which is based on GAAP are consistent with the IFRS-based ones.

According to four accounting harmonization approaches above, the accounting standards adopted by some countries or regions are exactly the same as IFRS issued by

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<sup>1</sup> The condorsement approach proposed by SEC does not imply that the United States will adopt this approach in the future, which is just one of the alternative mode of international financial reporting standards for future application.

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IASB and have not made any changes. Under other circumstances, those non-English-speaking nations or regions tend to adopt the translated version of IFRS with their own official languages. Since there might be some loss or inaccuracy in the translation, and linguistic differences in two languages are inevitable, the application and comprehension of the translated IFRS may well be different from its original English version. There are also some nations or regions that provide detailed guidelines for addressing specific issues for problems in certain industries. Those will modify or add individual IFRSs in order to incorporate them out of different intentions. Under the endorsement approach, if the country or region don't make any changes when adopting IFRS, the result is exactly the same as the direct adoption approach, which is fully adoption of IFRS. The endorsement approach proposed by the U.S. SEC is the integration of convergence approach and endorsement approach. (Min, Jianqiao, & Huaxin, 2010)



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## **4. IFRS adoption in transition countries – evidence of China**

### **4.1 Transition countries**

Transition countries refers to those nations that transform into a market-oriented economy from the original centrally-planned economy. Those countries have experienced a series of structural transformations which aim at developing a more reasonable economic system based on the market. Specifically, it means merchandise's price is decided by the supply and demand in the market instead of controlled by the government. Other changes include removing the barriers of trade, promoting the privatization process of nationalized resources and business, and establishing the financial department for the achievement of macroeconomic stability. (Feige, 2011)

Usually, transition countries mean those countries in central Europe and eastern Europe affected by the former Soviet Union. Nowadays it has a wider range which also includes Asian countries like China and Vietnam whose economic system is transforming from planned economy to market – oriented economy. In 2000, according to the International Monetary Fund (IMF), the transition countries are as follows:

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Figure 2: transition countries

<b>Transition economies in Europe and the former Soviet Union:</b>					
<u>Central and Eastern Europe</u>					
Albania	Croatia	Macedonia	Serbia	Montenegro	Kosovo
Bosnia-Herzegovina					
<u>Commonwealth of Independent States</u>					
Armenia	Azerbaijan	Belarus	Georgia	Kazakhstan	Kyrgyzstan
Moldova	Russia	Tajikistan	Turkmenistan	Ukraine	Uzbekistan
<b>Transition economies in Asia:</b>					
Cambodia	Laos	China	vietnam	Mongolia	
<b>Transition economies in Africa:</b>					
Botswana					

Source: World Bank

To sum up, transition countries refer to the countries trying to change the fundamental elements in their constitutions based on market-oriented principles, which may have been originated from a post-colonial circumstance, a Latin American post-dictatorship, a highly governed Asian-style economy or an African nation with lagging economy. It is not easy to harmonize different accounting standards, especially in transition countries because there tends to be various in the accounting systems of them. Examples are the revolution outcomes in economy or politics of China, Russia and Poland. In addition, the accounting system is also greatly affected by new legislation.

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## 4.2 Capital market

A capital market is a place where money is transferred from savers to investors, for example, governments, companies and other groups. Those transition processes are under the supervision of regulators such as the securities and exchange commission (SEC) to prevent errors and fraudulent practices. (O'Sullivan & Sheffrin, 2003). The capital market has consisted of two parts: the primary and secondary market. The primary market refers to the stage for savers to sell new stocks or bonds to investors by the way of underwriting. Those investors are mainly different scales of governments who issue bonds only and business companies who issue both equity and bonds. Those long-term funds include the funds of sovereign wealth, hedge, and pension. (Michael, 1996)

Investment banks set a beginning price range for a given security and supervise its transaction to investors. Once the initial transaction is complete, a further transaction will be carried on the secondary market, where a large number of exchange transactions take place each day. In the secondary markets, traders or investors conduct the transactions directly over-the-counter or through the exchange. The presence of the secondary market let those investors from primary market much more willing to carry on their investments because of the high possibility for them to cash out their investments quickly as needed. The electronic trading system of modern capital markets is greatly based on computers. Most of them can only be accessed by the financial

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departments of the government and enterprises, still, some of them are open to the public. Thousands of such systems exist nowadays, a large part of them serve only a small portion of the whole capital market. These systems are conducted by several entities, including the government, investment banks and stock exchanges. Generally, these systems are globally available, yet they are often centrally located in those well-known financial centers worldwide, typically in Hong Kong, New York, and London.

### **4.3 ASBEs and its legal position**

The China ASBEs came out by summarizing the experience of accounting reforms in China and drawing on IFRSs. It adapted to the actual economic needs of China's further development and has been recognized by other countries or regions. The Chinese ASBEs are the significant components of Chinese national system of regulations and laws. ASBEs focus on major corporation transaction and accounting elements' reporting, measurement and the recognition, taking the records of accounting into consideration. Although it still exists some differences, ASBEs have achieved substantial convergence with IFRSs and have established a rock-hard foundation to achieve the equivalence with the universal accounting standards in the world.

Regarding its legal position, ASBEs are an integral part of China's law system. Compared with ASBEs, IFRS is not a regulatory system, but it can deeply impact and strongly bind the international capital market. According to Legislation Law of the

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People's Republic of China issued by National People's Congress, the framework of the legal system in China covers four levels:

Table 3: the framework of Legislation Law of the People's Republic of China

1. national law	shall be passed by the Standing Committee of the National People's Congress and signed by the President;
2. administrative regulation	Shall be approved by the Standing Committee of the State Council and issued by the Premier of the State Council;
3. local decrees	shall be promulgated by the State Council departments and announced by ministers;
4. autonomous decree and special decrees	Shall be issued by the State Council departments in the form of documents

Source: congressional-executive commission on China

When it comes to accounting standards, fundamental standards are included in the second level administrative regulations, which are announced and signed by Jin Renqing, the Minister of Finance. The exact guidelines, and application guidelines are special decrees issued by Jin Renqing as accounting documents. Therefore, ASBEs are mandatory for all enterprises in China and require them to implement. Otherwise, they are considered to be non-compliance. Although IFRSs are not a regulatory system, it is equivalent if a country or region announces to fully adopt IFRSs. China is a country which substantially converged to IFRSs in terms of accounting recognition,

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measurement, and reporting. Formulating and issuing accounting standards in the form of regulations is more conducive to the implementation of these standards. (Li, 2017)

#### **4.4 Connection between IFRSs and ASBEs**

In terms of the connection between ASBEs and IFRSs, not only are the overall structures consistent but also most of the issues correspond to each other. IFRSs consist of three parts: financial statement preparation framework, standards for international financial reporting and the corresponding interpretations. ASBEs have the same structure. The role basic standards of ASBEs are similar to the framework of IFRSs. They play a vital role in both accounting standards and are the basis for the formulation of specific standards. basic standards of ASBEs and framework of IFRSs formulate the financial reporting objectives, accounting basis, assumptions, etc. The specific standards of ASBEs and application guidelines cover the accounting treatment of various economic transactions, which are the same as the internal structure of IFRSs.

The specific standards of ASBEs are divided into general business standards, special business standards and reporting standards, which mainly stipulate the recognition, measurement, and reporting of all specific business activities. After ASBEs was issued, the implementation issues encountered in practice will be fixed in the form of regulatory documents of the Ministry of Finance, which are the same as those in the IFRSs system. It has been relatively stable after ASBEs are released. If the new business

appears in actual work, new standards and specific guidelines will be formulated to regulate it in accordance with established procedures, taking into account international convergence and further improvement of ASBEs.

Table 4: comparison between ASBEs and IFRSs

Accounting Standard for Business Enterprise	International Financial Reporting Standards
CAS1 Inventories	IAS 2 Inventories
CAS 2 Long-term equity investments	IAS 27 Separate Financial Statements
	IAS 28 Investments in Associates and Joint Ventures
	IAS 31 Interests in Joint Ventures
CAS 3 Investment properties	IAS 40 Investment Property
CAS 4 Fixed assets	IAS 16 Property, Plant and Equipment
	IFRS 5 Non-current Assets Held for Sale and Discontinued Operations
CAS 5 Biological assets	IAS 41 Agriculture
CAS 6 Intangible assets	IAS 38 Intangible Assets
CAS 7 Exchange of non-monetary assets	IAS 16 Property, Plant and Equipment
	IAS 38 Intangible Assets
	IAS 40 Investment Property
CAS 8 Impairment of assets	IAS 36 Impairment of Assets
CAS 9 Employee compensation	IAS 19 Employee Benefits
CAS 10 Enterprise annuity fund	IAS 26 Accounting and Reporting by Retirement Benefit Plans
CAS 10 Enterprise annuity fund	IAS 26 Accounting and Reporting by Retirement Benefit Plans
CAS 11 Share-based payment	IFRS 2 Share-based Payment
CAS 12 Debt restructurings	IAS 39 Financial Instruments: Recognition and Measurement
CAS 13 Contingencies	IAS 37 Provisions, Contingent Liabilities and Contingent Assets
CAS 14 Revenue	IAS 18 Revenue
CAS 15 Construction contracts	IAS 11 Construction Contracts
CAS 16 Government grants	IAS 20 Accounting for Government Grants and Disclosure of Government Assistance
CAS 17 Borrowing costs	IAS 23 Borrowing Costs
CAS 18 Income taxes	IAS 12 Income Taxes
CAS 19 Foreign currency translation	IAS 21 The Effects of Changes in Foreign Exchange Rates
	IAS 29 Financial Reporting in Hyperinflationary Economies
CAS 20 Business Combinations	IFRS 3 Business Combinations
CAS 21 Leases	IAS 17 Leases
CAS 22 Recognition and measurement of financial instruments	IAS 39 Financial Instruments: Recognition and Measurement
CAS 23 Transfer of financial assets	
CAS 24 Hedging	

CAS 25 Direct insurance contracts	IFRS 4 Insurance Contracts
CAS 26 Re-insurance contracts	
CAS 27 Extraction of petroleum and natural gas	IFRS 6 Exploration for and Evaluation of Mineral Resources
CAS 28 Changes in accounting policies and estimates, and correction of errors	IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors
CAS 29 Events occurring after the balance sheet date	IAS 10 Events after the Reporting Period
CAS 30 Presentation of financial statements	IAS 1 Presentation of Financial Statements
	IFRS 5 Non-current Assets Held for Sale and Discontinued Operations
CAS 31 Cash flow statements	IAS 7 Statement of Cash Flows
CAS 32 Interim financial reporting	IAS 34 Interim Financial Reporting
CAS 33 Consolidated financial statements	IAS 27 Separate Financial Statements
CAS 34 Earnings per share	IAS 33 Earnings per Share
CAS 35 Segment reporting	IFRS 8 Operating Segments
CAS 36 Related party disclosure	IAS 24 Related Party Disclosures
CAS 37 Presentation of financial instruments	IFRS 7 Financial Instruments: Disclosures
	IAS 32 Financial Instruments: Presentation
CAS 38 First time adoption of Accounting Standards for Business Enterprises	IFRS 1 First-time Adoption of International Financial Reporting Standards

Source: (List of IFRS Standards, 2017) (Deloitte, 2018)

In 2002, the IASB has changed the name of the International Accounting Standards into the IFRSs. It is based on investors' standpoint with the purpose to confirm accounting elements and major economic business issues. Although ASBEs are not called Chinese financial reporting standards, its starting point and concept are consistent with IFRSs. China's previous accounting system was mainly prescribed in the form of accounting subjects and accounting statements. It also covered the contents of accounting recognition and measurement, and reporting. (Chen, 2002)



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## **4.5 Differences between IFRSs and ASBEs**

### **4.5.1 Difference in content**

IFRSs don't involve accounting records, it mainly regulates accounting recognition, measurement, and reporting. Accounting titles are designed by the company itself and handled by accountants. Financial reports disclose the result of recognition and measurement which is the carrier to transmit accounting information to investors and other users. Then investors and other information users can know their company's financial position and operating results, further predict the company's future development trends, and make investment decisions. (Lin J. Z., 2001)

The new accounting standards ASBEs clarified the importance of the accounting recognition, measurement, and reporting which are involved in 156 accounting titles newly defined instead of appendices of guidance in order to achieve international convergence. Considering the situation in China nowadays, the specification for accounting records is still needed for the reason that it can make ASBEs more operational and facilitate the implementation of a comprehensive and accurate standard system. In the premise of not violating the provisions for recognition, measurement, and reporting in ASBEs, companies can add, split, or combine accounting titles according to their actual conditions. (Lin J. Z., 1998)

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#### **4.5.2 Related Party Disclosures**

IFRSs consider companies controlled by the state to be Related Party and consider the transactions of the related party to be connected with party transactions, IFRSs require full disclosure of related party in financial statements. IFRSs require full disclosure of related party in financial statements.

This requirement is not suitable for China's capital market because of its special economy system. There are a lot of enterprises owned by the state or enterprises dominated by state-owned capital China. As defined by IFRSs, most of these enterprises are recognized as related parties. However, these enterprises are independent legal entities and they are not related parties if there is no existence of investment or others relations. Therefore, ASBEs stipulate that if companies both owned by the state but they do not have control or joint control relations and don't have significant influence, they are not recognized as related parties.

#### **4.5.3 Impairment of Assets**

The non-current asset impairment like the impairment of intangible and fixed assets accrued by the company is allowed to be recoverable and record the current loss or profit under IFRSs. ASBEs consider that recoverable amount for impairment of non-current assets after impairment losses have been accrued is little or none. Therefore,

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impairment of assets is permanent and cannot be reversed once it is confirmed. IASB understands the requirements of China and hopes that CASC pays attention to the convergence of IFRSs and US GAAP because under US GAAP impairment of non-current assets are also not allowed to be reversed after impairment losses have been recognized.

#### **4.5.4 business combinations under common control**

There are two kinds of business combinations, which have been categorized into two classifications: the business combinations under or not under common control. under ASBEs. IFRSs only clarify the accounting treatments for those which are not under control. And those under control occur often because of China's special economic system. The IASB believes that the provisions and practices of ASBEs in this area will provide a useful reference for IFRSs.

#### **4.5.5 Fair value measurement**

The difference between IFRS and ASBEs lies in the point which part has to adopt the model of fair value. According to IFRS, an organization is allowed to freely adopt the fair value model or the cost model for the establishment of accounting policies. As regulated in Chinese Accounting Standard, only by presenting convincing evidence which can suggest the reliable and ongoing obtainment of the organizational investment

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properties' fair value of the market, can an organization adopt the fair value model. Fair value and historical cost are the most important measurements in accounting. Fair value works for the current period and the historical cost is for the past. Fair value measurement is widely used under IFRSs in order to fully reflect the relevant accounting information.

CASC decided to put fair value measurement moderately into use for the consideration of China's incomplete capital market. As an emerging market country, China doesn't have a well-built active market for all assets. Although the relevance of accounting information is important, there's high probably to come out artificially manipulated profits if China adopts IFRSs fair value measurement directly. Therefore, the fair value measurement of debt restructuring, non-monetary assets, biological assets and investment properties can only be performed under ASBEs if it is available to China's active market, and if there are the reliable obtainment and measurement of the fair value.

#### **4.5.6 Non-current Assets Held for Sale and Discontinued Operations**

The accounting method of disposal to the non-current assets held for sale and discontinued operations have been separately stipulated by IFRS 5. As a result, the Non-current assets generally are the intangible and fixed assets, and the discontinued operations refer to the disposal of the company's workshops, branches, subsidiaries, etc., which are ready for sale. Under IFRS, if a company makes a decision on the disposal

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of its non-current assets and the termination of operations,

Those conditions below have to be considered at first:

- the management has made commitments and is willing to sell the assets;
- the assets can be sold immediately;
- the organization has started a program to find an asset buyer;
- the assets are greatly likely to be sold in one year (except for those limited items);
- there is the active marketing ongoing for the assets and the price of the asset shall be reasonably made based on the fair value of them;
- necessary actions have to be taken to ensure that there will be no possible changes or withdrawal of this sales plan;

then the non-current asset will be transferred into current assets, its depreciation or amortization shall be stopped, measured as the sales cost with lower fair value and carrying amount. If book value proves to be higher than the sales cost with lower fair value, then the extra amount will be recorded in current loss or profit. ASBEs mention non-current assets held for sale and discontinued operations in CAS 4 Fixed assets and CAS 30 Presentation of financial statements instead of formulating separately.

#### **4.5.7 Employee Benefits**

“IAS 19 Employee Benefits” and “IAS 26 Accounting and Reporting by Retirement

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Benefit Plans” make specifications about the fundamentals of the disclosure and measurement of the retirement benefit plan reports about defined contribution plan and Defined benefit plan. As China's current laws and regulations do not have similar provisions for defined benefit plan, ASBEs only have specified the basic old-age insurance and supplementary endowment insurance. (Lorenzo, 2016)

#### **4.5.8 Financial Reporting in Hyperinflationary Economies**

IFRS 29 can be applied to the circumstance where the currency in a highly inflationary economic environment serves as the functional currency of an organization. According to the standard, the restatement needs to be made about the financial statements and the relevant historical data of an organization with highly inflationary functional currency to change the currency’s general power of pricing. ASBEs assume that China is not expected to experience hyperinflation under its special market economy, therefore, there is no need to formulate such guidelines. According to the requirement of ASBEs, this restatement has to be made according to the general price index.

#### **4.5.9 Investment property**

Under ASBEs, investment properties refer to the extra item added to a balance sheet for separate presentation. The same cost model can be applied to these properties as that of the fixed assets, which need to be depreciated, or other long-term assets, which need to

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be amortized among the developers of the properties. If the continuously reliable determination of the investment property's fair value can be obtained, the fair value model is able to be put into practice. By applying the fair value model, the amortization and depreciation won't be presented. The direct recognition of the carrying amount's difference from fair value is presented in loss or profit. (Lorenzo, 2016)

In my opinion, based on the summary of the reasons for international accounting difference, the reasons caused the difference between IFRSs and ASBEs can be drawn as the standard- setting boards, the orientation of setting standards, and the objective users. Firstly, China is a country which applies code law system, which means its accounting practices and financial reporting regulations are formulated by the government instead of independent professional institutions like IFRSs. Secondly, the orientation of setting ASBEs is based on rules. However, IFRSs are based on principles. Last but not least, ASBEs takes all enterprises except financial enterprises and small enterprises in China into consideration which shows a strong tendency. Instead, IFRSs are designed with the purpose of the wider range of application. Although ASBEs and IFRSs still have many differences above, some of them are possible to converge for further adoption.

#### **4.6 International convergence of ASBEs**

A nation is able to adopt IFRSs to begin with, and then to accordingly make some

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adjustments and variations, which is exactly what China has done. From the year 2007, the listed enterprises in China have been required to adopt the IFRS-based standards in their consolidated statements. However, some obvious differences also exist. For instance, the impairment is irreversible, which is different from the requirement of IAS 36. And a different kind of adoption has been presented in Venezuela, which started to use IFRSs in the year of 2004, yet didn't adopt all its changes subsequently.

China's Ministry of Finance and the Accounting Standards Committee established a close cooperative relationship with the International Accounting Standards institution in 1990. After signing the "Joint Statement on the convergence of China Accounting Standards and International Financial Reporting Standards" on 8/11/2005, the International Accounting Standards Board and the Ministry of Finance have established a mechanism for continuous convergence by meeting regularly and exchanging specialists and experts.

Remarkable results of the international accounting standard have been yielded in China with years of unremitting efforts. In 2004, the Ministry of Finance proposed the "Four Principles" of accounting for international convergence, that is, convergence is the direction, the process, the interaction, and not exactly the same. For example, based on the actual situation of China's capital market, China's accounting standards set more stringent restrictions than international on fair value. Due to the large number of state-owned enterprises, China's accounting standards are also slightly different from



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international standards in the disclosure of related parties of state-owned enterprises. The international standards will revise its related party disclosure guidelines with reference to the actual Chinese situation.

According to China's Ministry of Finance, the representatives of the IFRS Foundation Trustees held a 4-day bilateral meeting in 10/2015, and it was the Assistant Minister of the Chinese Ministry of Finance, Dai Bohua and the Chairman of the IFRS Foundation Trustees who led this meeting.<sup>2</sup> On this meeting, the notable success of the Beijing Joint Statement (issued in 11/2005 by IASB and CASC) was emphasized by both sides. From the perspective of both sides, the expected goals of the Beijing Joint Statement have been well obtained. Particularly, the sustainable convergence of CAS with IFRS, and the application of these converged standards have achieved significant enhancement on the transparency and quality of Chinese financial reporting.

What's more, the notable process was also emphasized by both sides in order to establish IFRS to be the single set of international and high-quality standards for accounting and the resultant changes in the global landscape of financial reporting. With the recognition of the progress that has so far achieved, both sides reach a consensus that it is the high time to update the 2005 Beijing Joint Statement for the reflection of both the Chinese and global process, and to establish the basis for further

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<sup>2</sup> Ministry of Finance of China and IFRS Foundation joint statement, 18 November, 2015, Beijing

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collaboration in the future.

#### **4.6.1 Emphasizing the goal of full convergence**

After a decade of the unceasing collaboration on IFRS since the initiation of the 2005 Beijing Joint Statement, which was led by Lou Jiwei, the Finance Minister, Dai Bohua made a reaffirmation that China is continuously committed to the endeavors of the IFRS Foundation, the aim endorsed by G20 at the single set of international and high-quality standards of accounting and China's vision of obtaining this aim via converged standards with IFRS. The goal of full convergence conforms to the development and reform of China.

#### **4.6.2 Enhancing continued cooperation**

The representatives of the Trustees appreciated a lot that China has presented an effective leadership of the Secretariat of the IASB's Emerging Economies Group. In addition to this, China has participated in all kinds of consultative institutions or working teams, has involved in the various advisory bodies and consultative working groups, and has both technologically and financially supported the IFRS Foundation. According to the representatives of the Trustees, they will continuously make sure that the full involvement of the Chinese interested parties will be guaranteed into the IFRS development in the future, which is firmly in line with the G20 request of deepening

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the emerging economies' participation into the endeavors of the IASB and the IFRS Foundation.

#### **4.6.3 Establishing a joint working group for further cooperation**

Based on the obtained success, both sides intend to explore the potential approaches to further applying IFRS in Chinese entities. To obtain this goal, both sides agree to form a joint work team aiming at the exploration of these approaches for further IFRS application in Chinese entities and other relevant problems, particularly targeting those Chinese corporations with international orientations. Shortly after this plan was made, the very first meeting about this joint working team is going to be held.

Other differences reflect in some adjustments made by CASC for better adoption of IFRSs. The first is to divide “IAS 39 Financial Instruments: Recognition and Measurement” into three standards: the recognition and measurement of financial instrument, hedging, and financial assets transfer, segmenting complex financial instruments for better guidance in practice. Secondly, “IFRS 4 Insurance Contracts” is divided into two standards, the original insurance contract and the reinsurance contract. ASBEs clarify more detailed and systematic principles on recognition, measurement and reporting of insurance contracts. The third is to integrate the relevant content of “IAS 27 Separate Financial Statements”, “IAS 28 Investments in Associates and Joint Ventures” and “IAS 31 Interests in Joint Ventures” to form the guideline of the equity

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investment in the long run and the application of this guideline, while IAS 31 has been replaced with “IFRS 11 Joint Arrangements” and “IFRS 12 Disclosure of Interests in Other Entities”, which will be put into practice on or after 01/01/2013.

## **4.7 China’s capital market**

In 2011, the Central Economic Work Conference formed that next stage of China's development direction for industry economy should follow the strategy to emphasize both the real economy and the virtual economy. While optimizing and upgrading the manufacturing industry, China must give great support to develop the financial industry. To be specific, industrial structure upgrading will promote the transformation of industries from low-end to high-end and the development of strategic emerging industries. To take the road of new industrialization, those cannot work without the sustainment from capital market.

There are two types in the capital market of China which are called A shares and B shares. According to the laws, Chinese listed enterprises are allowed to issue either A or B or both shares in Shanghai Stock Exchange (SHSE) and Shenzhen Stock Exchange (SZSE). The domestically listed enterprises in Chinese are required to issue Chinese-currency-denominated shares. The trade of A shares is only allowed to be conducted in the stock market of China among Chinese investors. When a Chinese listed enterprise is looking forward to raising foreign funds, it will have to submit application for B

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shares issuance, whose quotations are foreign currencies (HK Dollar in the SZSE and US Dollar in the SHSE).

Before 01/01/2001, B share trades were exclusive to foreign investors, but with the change of the regulation, now Chinese investors are also allowed to take part in it. (Kuan, 2007) On the other hand, it also allow the share issuance of Chinese listed enterprises in foreign market. Therefore, there is another type of stock, H shares, which are issued by Chinses listed enterprises and traded in HKSE, where the majority of trades of Chinese offshore stocks happen. H shares are denominated in HK Dollar. Different from the situation of the previous two types of shares, H shares has no specific requirements for the trading residents.

As for the enterprises which have issued A shares in the market, they need to submit reports annually in accordance with ASEBs to an appointed CPA company by the CSRC for auditing. Before the year of 2007, as for the enterprises which have issued B shares, they needed to submit reports annually based on IAS to big global accounting companies (e.g. Big Four) for auditing. Reconciliation will be required if there is difference between the IFRS-based and ASBE-based net revenue. With the 2006 version being implemented to all enterprises listed in mainland China, as announced in 10/2007 by CSRC, “the foreign-capital enterprises listed in the stock market of mainland China (known as B-share enterprises) don’t need to be double audited offshore and in mainland China any longer” as the standards for the auditing and

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accounting in China conform more and more to the global practices. Besides, those B-shares enterprises will be free to choose audit companies on the basis of their own demands.

Because of the requirements for listed enterprises, the enterprises which have issued H shares need to submit their reports in accordance with HKFRSs OR IFRSs to globally famous accounting companies like Big Four for auditing. With a long-time effort to converge with IASs, the full harmonization of HKFRSs with IFRs has almost been achieved by 2005, with the exception of several tiny differences. “The fact that HKFRS has been increasingly converged with IFRS further supports the reports of H-share enterprises to serve as a benchmark in the comparative study. By comparatively analyzing the reports of H-share and A-share enterprises, more insight will indeed be provided into the Chinese harmonization process.

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## 5. Development of research methodology and hypothesis

### 5.1 Methodology

Practical part of this thesis will focus on the analysis of IFRSs adoption in the firm level. In particular, there will be assessed the relationship between IFRSs adoption and capital market indicator such as return on net asset and comparability index.

According to Gray (1980)'s research on the influence from International Accounting Differences from a Security-Analysis Perspective, a commonly used index for testing the convergence of accounting standards is "Conservatism" Index which requires the sample company's net profit and return on net asset. Recently, the index has been referred to as "comparability index", which is applied in the comparison of the numbers in one company's accounting reports based on various accounting standards. Formulation of comparability index between the defined criteria is:

$$\text{Comparability index} = 1 - \left( \frac{R_A - R_D}{|R_A|} \right)$$

where  $R_D$  refers to the disclosed profit and  $R_A$  refers to the adjusted profit. After adjusted to the research of this thesis, comparability index between IFRSs and ASBEs is:

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$$\text{Comparability index} = 1 - \left( \frac{\text{net income}_A - \text{net income}_H}{|\text{net income}_A|} \right)$$

Among them: net income A refers to the sample company's net income under ASBEs and net income H refers to the sample company's net income under IFRSs. It's obviously seen in the equation that comparability index will be 1.0 when net income A equal net income H. When the reported ASBEs net income is at least 10% greater than the reported IFRSs net income, the value of comparability index will be 0.90 or below. Similarly, when the reported ASBEs net income is at least 10% less than the reported IFRSs net income, the value of comparability index will be 1.10 or above.

According to Haverty (2006)' s further study on Gray's comparability index, 5% of materiality were set to measure if financial reporting under IFRSs were comparable to that under another accounting standard, that means, if the average comparability index were between 0.95 and 1.05, the results are convergent. (Haverty, 2006) Here in this thesis, we assume that 10% of materiality will be set to measure if the reported IFRSs net income are comparable to the reported ASBEs net income. Therefore, if the average comparability index is between 0.90 and 1.10, it is considered that reported IFRSs net income and the reported ASBEs net income are convergent. There are also some flaws of the comparability index, one of which is that when the denominator gets close to 0, the value of comparability index goes extreme. However, the merit of this



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comparability index lies in the fact that it highlights the material differences, if any, between these two net incomes.

## **5.2 Hypothesis**

From the analysis above, we can see that great endeavors have been made in China to converge with IFRSs. Nonetheless, there are also some concerns on the applicability of IFRSs to Chinese accounting practices. The thesis here aims at evaluating the degree to which the IFRS-based accounting measurements of the listed enterprise of China are comparable to the ASBEs-based ones. Given the highly convergence between IFRSs and ASBEs, the improvement of the comparability reflected in the reduction of the comparability index between the reported IFRSs net income and the reported ASBEs net income can be obviously noticed.

According to an annual report sample from the listed enterprises of China with the issuance of both H and A shares in 2005, 2006, and 2007, this thesis aims to evaluate the extent to which the comparability index has been reduced. The calculation of the comparability index was performed on an annual basis of every corporation in this study. Besides, the calculation of the average value of the comparability index during all these years was also performed for every corporation in this study. Furthermore, based on another set of sample companies' annual reports issued from 2008 to 2017, return on net assets will be analyzed to measure sample companies'

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financial performance.

**Question:**

(1) What is the average comparability index between the financial statements respectively based on IFRSs and ASBEs of listed enterprises who issue both A share and H share? Does the result show convergence between ASBEs and IFRSs?

**Outcome a)** average comparability index are between 0.90 and 1.10, the reported IFRSs net income and the reported ASBEs net income are convergent.

**Outcome b)** average comparability index are under 0.90 or over 1.10, the reported IFRSs net income and the reported ASBEs net income do not show convergence.

(2) Does adoption of IFRSs have positive or negative effect on listed enterprises with the issuance of both H and A shares?

**Outcome a)** the return on net assets will decrease/increase with the IFRSs adoption

**Outcome b)** no impact

### **5.3 Sample selection**

Till now, there have been 95 enterprises in total which have been listed both in the stock markets of Hong Kong and mainland China, whose industry category distribution are shown in table 5. The increasing number shows China's listed companies have gradually raised funds through overseas capital markets and broadened the financing

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channels which is of great importance to Chinese economic prosperity. It also reflects the accounting harmonization's importance that it will help reduce the cost of investors and increase the transparency of the accounting information of listed companies.

Table 5: industry category of enterprises which have been listed both in the stock markets of Hong Kong and mainland China

Industry Category	number
financial service	17
transport	15
automobile making	5
special-purpose equipment	5
nonmetal	4
oil exploitation	4
general-purpose equipment	4
civil engineering	4
pharmaceutical manufacturing	4
electric heating	3
ferrous metal	3
Insurance	3
coal mining and processing	3
electric apparatus	2
electronic equipment	2
real estate	2
metalware	2
fuel	2
nonferrous metals	2
textile and apparel	1
utilization of debris	1
commercial services	1
retail	1
food processing	1
water supply	1
media	1
beverage	1
paper products	1

Source: Hong Kong Exchange and Shanghai Stock Exchange

this thesis chose Xinjiang Goldwind, BYD, CITIC Securities, PingAn Insurance Company of China, China Life Insurance Company and other listed companies from

different industries randomly among 95 companies as the sample companies to analyze comparability index. the results of the comparability index of 15 listed companies in 2005, 2006 and 2007 which simultaneously issued both H and A shares have been illustrated in the table.

Table 6: comparability index of sample companies in 2005,2006 and 2007

	net income under CAS(RMB)			net income under IFRS(RMB)		
	2005	2006	2007	2005	2006	2007
Xinjiang Goldwind Sci & Tech		319,584,000.63	634,716,500.48		318,254,880.87	604,603,289.85
BYD	368,433,000.00	1,020,921,000.00		252,332,000.00	-39,691,000.00	
HUANENG Power	5,573,638,529.00	6,445,419,763.00	6,417,605,258.00	4,780,468,882.00	5,579,385,045.00	6,205,051,075.00
ANHUI EXPRESSWAY	658,194,755.49	761,792,090.91	604,653,255.68	659,248,355.31	749,302,455.39	471,528,781.83
COSCO Shipping Energy Transportation	2,716,964,553.83	2,763,790,541.08	4,596,050,561.15	2,691,091,018.11	2,741,108,424.44	3,724,491,711.31
Huadian Power	1,104,616,000.00	1,288,079,000.00	1,547,009,000.00	1,014,976,000.00	1,121,886,000.00	928,182,000.00
Sinopec	42,460,000,000.00	51,360,000,000.00	57,153,000,000.00	39,531,000,000.00	50,151,000,000.00	54,683,000,000.00
China Southern Airlines	-1,769,000,000.00	170,000,000.00	2,039,000,000.00	-1,794,000,000.00	118,000,000.00	1,642,000,000.00
China Eastern Airlines	24,939,156.83	-2,699,222,120.76	610,831,000.00	37,454,094.30	-2,736,194,658.13	693,271,000.00
Yanzhou Coal	2,495,957,448.00	1,749,682,583.00	2,690,958,566.00	2,495,481,451.00	1,758,212,857.00	2,868,216,070.00
CITIC Securities	329,617,781.18	2,488,993,433.09	13,545,785,865.29	400,041,572.70	2,371,040,863.82	8,258,879,687.66
Ping An Insurance Company of China	3,368,153,000.00	6,122,748,000.00	15,581,000,000.00	3,338,428,000.00	5,996,818,000.00	6,862,000,000.00
China Life Insurance Company	5,514,000,000.00	9,693,000,000.00	28,297,000,000.00	5,456,000,000.00	9,601,000,000.00	27,922,000,000.00
Haitong Securities		457,374,591.01	5,560,130,959.59		411,382,861.62	5,353,325,674.47
Orient Securities		936,148,982.67	4,303,174,897.91		1,421,446,499.83	4,302,524,190.37

	C index			average C index
	2005	2006	2007	
Xinjiang Goldwind Sci & Tech		1.00	0.95	0.97
BYD	0.68	-0.04		0.32
HUANENG Power	0.86	0.87	0.97	0.90
ANHUI EXPRESSWAY	1.00	0.98	0.78	0.92
COSCO Shipping Energy Transportation	0.99	0.99	0.81	0.93
Huadian Power	0.92	0.87	0.60	0.80
Sinopec	0.93	0.98	0.96	0.95
China Southern Airlines	0.99	0.69	0.81	0.83
China Eastern Airlines	1.50	0.99	1.13	1.21
Yanzhou Coal	1.00	1.00	1.07	1.02
CITIC Securities	1.21	0.95	0.61	0.93
Ping An Insurance Company of China	0.99	0.98	0.44	0.80
China Life Insurance Company	0.99	0.99	0.99	0.99
Haitong Securities		0.90	0.96	0.93
Orient Securities		1.52	1.00	1.26

Source: each companies' annual reports in 2005, 2006 and 2007

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From the results of average comparability index, we can see that nine of them are between 0.90 and 1.10, following the method above, it is considered that the reported IFRSs net income and the reported ASBEs net income are convergent. However, we cannot summarize that result the two accounting standards are convergent because the lack of enough and sufficient statistics of reported ASBEs net income and reported IFRSs net income from the same company, also the time when those companies went public differ from each other.

Another influencing factor is the notice of “Insurance Industry's Implementation of the Interpretation No. 2 of the Accounting Standards for Business Enterprises” (hereinafter referred to the “Interpretation No. 2”). On August the 7<sup>th</sup>, 2008, the Ministry of Finance issued the Interpretation No. 2, requiring the recognition, measurement and reporting of the same transaction of all the public companies listed at mainland China and abroad by adopting the same accounting estimate method and policies. For the companies both issue A share and H share, Interpretation No. 2 requires them to apply the same accounting policies and accounting estimate method to recognize, measure and report their financial activities after ASBEs and HKFRSs get equivalent, except for the long-term assets’ impairment and related parties disclosure. It implies that the reported IFRSs net income equals the reported ASBEs net income, which has been reflected in the value of comparability index as 1.0. This is a significant evidence to show convergence between ASBEs and IFRSs.

## 5.4 Return on Net Assets

Another method to measure a corporation's performance comparatively with that of its competitors is known as Return on net assets (RONA). RONA is used to measure the corporate performance in terms of finance, which tells whether the corporation is deploying assets to create economic values or not. To get accurate results, the unusual events which are likely to influence the outcomes need to be left out. When the RONA is high, it indicates the excellence in the corporate performance. The RONA calculation should be performed as follows:

$$\text{RONA} = \frac{\text{net income}}{\text{fixed assets} + \text{net working capital}}$$

$$\text{Net working capital} = \text{Current Assets} - \text{Current Liabilities}$$

Eight companies are chosen randomly as sample companies to analyze RONA. The calculations are shown from table 7 to table 14.

Table 7: RONA of Weichai Power (blue line)

WEICHAI POWER	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	1,637,920,692.68	1640084580	8,777,694,348.24	7,659,832,894.31	0.59
2009-12-31	2,829,578,632.74	1777100218	11,719,859,704.42	7,887,986,888.02	0.50
2010-12-31	5,766,926,153.83	1846271419	17,355,922,939.36	11,323,878,579.42	0.73
2011-12-31	5,116,932,142.65	1998819919	22,059,320,092.53	12,832,603,635.12	0.46
2012-12-31	3,643,539,237.76	2223533259	21,474,532,839.00	9,365,305,131.00	0.25
2013-12-31	3,830,948,677.86	2612062853	27,396,084,786.02	13,945,219,150.65	0.24
2014-12-31	3,685,192,565.78	2620753453	27,921,045,470.71	14,139,642,506.67	0.22
2015-12-31	1,688,368,108.53	2644294727	23,447,030,134.14	9,890,744,734.79	0.10
2016-12-31	2,987,506,866.74	2985724486	28,769,802,954.40	13,712,078,739.66	0.17
2017-12-31	6,168,118,818.68	3043915671	40,821,787,669.04	23,469,082,747.68	0.30

Source: annual reports of Weichai Power from 2008 to 2017

Table 8: RONA of Zoomlion Heavy Industry

Zoomlion Heavy Industry	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	1,543,754,052.06	1089461691	10,280,281,135.15	7,151,044,718.39	0.37
2009-12-31	2,400,771,460.67	1888413964	15,736,148,178.85	11,706,209,278.92	0.41
2010-12-31	4,433,007,379.18	2418483646	42,560,324,937.07	19,971,994,006.48	0.18
2011-12-31	7,504,370,000.00	2914760000	47,210,630,000.00	21,659,870,000.00	0.26
2012-12-31	6,503,202,770.54	3316527591	52,418,990,713.52	27,108,056,612.25	0.23
2013-12-31	2,885,477,138.78	3682208049	56,755,000,638.42	29,206,214,650.08	0.09
2014-12-31	45,921,820.62	4019132345	58,926,614,689.31	24,070,206,024.88	0.00
2015-12-31	109,634,506.18	4398646738	55,942,927,575.79	25,109,865,399.63	0.00
2016-12-31	212,366,555.87	4096190682	57,286,273,110.14	24,862,982,458.41	0.01
2017-12-31	256,232,073.75	2834381933	55,551,763,274.37	24,556,975,231.44	0.01

Source: annual reports of Zoomlion Heavy Industry from 2008 to 2017

Table 9: RONA of Jingwei Textile Machinery

Jingwei Textile Machinery	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	70,165,884.44	462869108.5	2,568,943,383.56	1,541,267,462.19	0.05
2009-12-31	63,284,714.04	365944112	3,129,942,837.33	1,658,214,172.06	0.03
2010-12-31	12,381,104.48	325408766.8	4,195,116,622.82	4,276,304,186.21	0.05
2011-12-31	116,239,230.81	319846235.5	3,520,925,515.05	4,278,052,336.01	(0.27)
2012-12-31	17,046,094.71	275654722.5	4,186,866,277.88	3,210,089,786.47	0.01
2013-12-31	53,601,488.77	260278734.3	4,117,636,282.65	3,815,366,012.06	0.10
2014-12-31	17,912,619.01	273148587.3	4,002,534,314.03	3,807,716,516.15	0.04
2015-12-31	57,387,484.87	252147256.6	4,330,450,900.35	4,404,735,086.61	0.32
2016-12-31	37,660,992.61	248261624.1	4,354,164,192.91	4,405,922,458.13	0.19
2017-12-31	344,755,500.18	222832020.4	3,200,806,702.16	3,926,424,918.32	(0.69)

Source: annual reports of Jingwei Textile Machinery from 2008 to 2017

Table 10: RONA of Northeast Electric Development Company

Northeast Electric Development Company	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	(109,883,144.87)	1605673.57	598,881,716.11	275,961,593.86	(0.34)
2010-12-31	(5,660,306.94)	564689.27	432,967,946.33	81,663,692.47	(0.02)
2011-12-31	(61,105,646.18)	461571.54	388,952,600.72	81,481,931.82	(0.20)
2012-12-31	7,801,856.01	324390.45	364,629,582.81	80,213,805.81	0.03
2013-12-31	4,804,434.13	242267.37	354,282,542.15	88,142,240.94	0.02
2014-12-31	(154,607.83)	81148.52	363,643,249.08	97,496,436.85	(0.00)
2015-12-31	(1,620,225.22)	23528.65	343,445,872.95	78,861,666.07	(0.01)
2016-12-31	(9,131,252.84)	47828.87	308,290,219.25	52,861,572.31	(0.04)
2017-12-31	(377,145,943.25)	46373.6	273,339,829.88	330,950,838.07	6.55

Source: annual reports of Northeast Electric Development Company from 2008 to 2017

Table 11: RONA of ZTE Corporation

ZTE Corporation	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	977,862,000.00	2,608,957,000.00	39,549,250,000.00	31,199,541,000.00	0.09
2009-12-31	733,826,000.00	3,195,746,000.00	53,060,986,000.00	45,175,437,000.00	0.07
2010-12-31	323,088,000.00	4,253,887,000.00	62,022,755,000.00	54,587,615,000.00	0.03
2011-12-31	503,793,000.00	4,791,141,000.00	81,101,055,000.00	78,110,937,000.00	0.06
2012-12-31	(1,427,799,000.00)	5,083,046,000.00	83,289,539,000.00	85,046,992,000.00	(0.43)
2013-12-31	375,923,000.00	4,751,559,000.00	77,738,811,000.00	77,366,309,000.00	0.07
2014-12-31	1,558,172,000.00	4,458,748,000.00	78,879,679,000.00	83,507,104,000.00	(9.24)
2015-12-31	2,536,966,000.00	4,340,067,000.00	93,675,981,000.00	89,572,450,000.00	0.30
2016-12-31	(4,224,145,000.00)	4,508,652,000.00	102,724,938,000.00	109,664,653,000.00	1.74
2017-12-31	6,051,419,000.00	4,887,175,000.00	98,977,166,000.00	97,998,789,000.00	1.03

Source: annual reports of ZTE Corporation from 2008 to 2017

Table 12: RONA of Ansteel

ANSTEEL	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	2,981,000,000.00	43252000000	19,913,000,000.00	21,323,000,000.00	0.07
2009-12-31	772,000,000.00	51720000000	21,416,000,000.00	32,435,000,000.00	0.02
2010-12-31	2,123,000,000.00	53744000000	27,448,000,000.00	32,174,000,000.00	0.04
2011-12-31	(1,968,000,000.00)	50337000000	25,250,000,000.00	32,526,000,000.00	(0.05)
2012-12-31	(3,731,000,000.00)	48161000000	25,942,000,000.00	39,161,000,000.00	(0.11)
2013-12-31	232,000,000.00	45405000000	28,643,000,000.00	37,388,000,000.00	0.01
2014-12-31	973,000,000.00	45983000000	24,784,000,000.00	36,024,000,000.00	0.03
2015-12-31	(4,597,000,000.00)	50399000000	21,685,000,000.00	41,823,000,000.00	(0.15)
2016-12-31	1,661,000,000.00	48233000000	24,694,000,000.00	36,145,000,000.00	0.05
2017-12-31	5,365,000,000.00	46290000000	26,365,000,000.00	31,835,000,000.00	0.13

Source: annual reports of Ansteel from 2008 to 2017

Table 13: RONA of Shangdong Xinhua Pharmaceutical

SHANDONG XINHUA PHARMACEUTICAL	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	30,515,020.65	862059705.2	768,330,303.17	625,610,382.22	0.03
2009-12-31	98,893,086.53	792722287.1	957,834,464.71	496,479,227.93	0.08
2010-12-31	65,484,666.97	745077549.5	997,551,940.10	592,464,337.74	0.06
2011-12-31	74,231,095.62	702928789	1,035,019,484.76	765,861,206.47	0.08
2012-12-31	55,888,333.92	925888204.2	1,376,404,688.74	790,564,272.43	0.04
2013-12-31	39,441,754.49	911119730	1,417,980,175.41	816,923,513.18	0.03
2014-12-31	28,309,964.04	1387022720	1,369,349,293.24	1,358,530,047.99	0.02
2015-12-31	41,516,976.29	1503751384	1,602,945,569.86	1,782,285,108.49	0.03
2016-12-31	77,523,616.79	1541339434	1,589,591,312.74	2,054,193,644.09	0.07
2017-12-31	142,916,897.12	1584557780	1,712,715,964.01	1,175,225,685.65	0.07

Source: annual reports of Shangdong Xinhua Pharmaceutical from 2008 to 2017

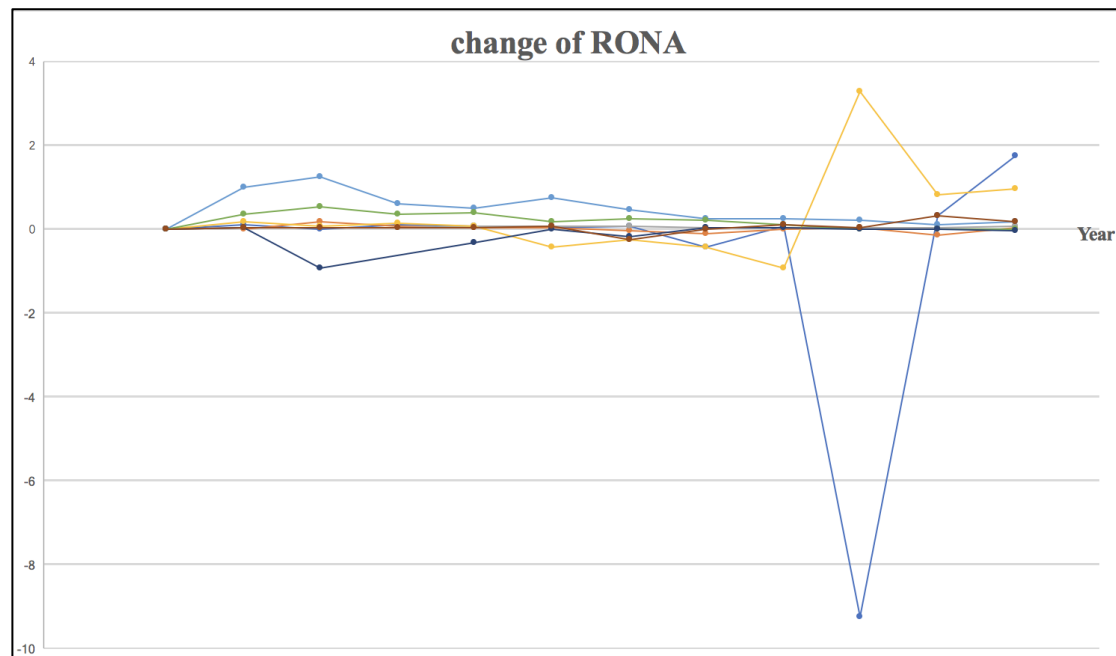


Table 14: RONA of Hisense Kelon Electrical

Hisense Kelon Electrical	net income	fixed assets	current assets	current liabilities	RONA
2008-12-31	(254,539,273.08)	332620634	2,460,737,380.43	4,469,790,703.88	0.15
2009-12-31	(122,220,123.14)	289189805.5	2,176,710,169.05	4,403,445,494.77	0.06
2010-12-31	612,391,390.48	250115718.9	3,755,591,683.45	5,430,286,773.26	(0.43)
2011-12-31	246,020,866.58	211015835.2	4,024,527,726.67	5,227,092,433.23	(0.25)
2012-12-31	336,604,324.71	184855845.7	4,730,456,072.49	5,672,829,625.08	(0.44)
2013-12-31	527,264,002.07	170557944.2	6,608,276,873.50	7,344,199,365.56	(0.93)
2014-12-31	964,079,696.22	136178710.7	3,050,739,339.88	2,894,421,008.43	3.30
2015-12-31	579,474,563.01	120208519.7	2,909,661,756.05	2,335,475,827.76	0.83
2016-12-31	730,672,506.63	43579821.24	1,483,357,545.87	778,639,076.40	0.98
2017-12-31	1,466,501,221.64	30816121.41	2,123,334,651.18	1,018,999,097.08	1.29

Source: annual reports of Hisense Kelon Electrical from 2008 to 2017

Graph 1: changes of RONA



From the figure 3 above, we can see that since Interpretation No. 2 of ASBEs has been introduced, the results of those sample companies tend to be stable in general except for Hisense Kelon Electrical's (blue line) sudden increase in 2015 and ZTE Corporation's sharp decrease (yellow line) in 2015. The adoption of IFRSs has a positive impact on China's capital market.

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Through the empirical analysis and test of the 12 listed enterprises with the simultaneous issuance of both H and A shares, we can draw the conclusion that, although ASBES haven't fully converged to IFRSs, China shows great interest to adopting IFRSs and introducing it to China's capital market. Gradual notices and interpretations of accounting standards are the result and reflection of the international coordination and convergence efforts of accounting standards, and it also marks a milestone in the reform of China's accounting standards. As the gap between ASBES and IFRSs narrows down, the adjustments that companies in mainland China need to adopt will also gradually decrease, even afterwards.

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## 6. Conclusion

### 6.1 Findings

The thesis here has made deep exploration of the harmonization of China's ASBEs with IFRSs, and concentrates on the differences and the connections on the basis of specific accounting standards. From our research, the findings can be concluded as follows:

- (1) The reasons cause international accounting difference can be the several differences in legal system, economic levels, culture difference and financing sources. To overcome these obstacles come from international accounting difference, accounting harmonization is necessary for every country for the advantages of the enhancement of comparability and market efficiency, the promotion of global integration, the unification of business transactions, and the improvement of transparency. As a result, nearly 120 countries and regions in the world have requested or permitted the adoption of IFRSs or convergence with IFRSs. There are three approaches primarily to applying IFRSs: direct adoption approach, convergence approach, and endorsement approach. U.S. SEC introduced the forth one condorsement approach.
- (2) ASBEs puts emphasis on recognizing, measuring and reporting the major economic affairs in business and accounting elements, considering what's been required by

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accounting records. Accounting records do not belong to IFRSs, which mainly regulates accounting recognition, measurement and reporting. Accounting titles are designed by the company itself and handled by accountants. ASBEs involved in 156 accounting titles newly defined instead of appendices of guidance in order to achieve international convergence. Other differences appear in related party disclosures, impairment of assets, business combinations under common control, fair value measurement, employee benefits, financial reporting in hyperinflationary economies and investment property. Considering the situation in China nowadays, specification for accounting records is still needed for the reason that it can make ASBEs more operational and facilitate the implementation of a comprehensive and accurate standard system.

(3) Adopting IFRSs for China's businesses has a direct and indirect impact, direct impact is reflected in favor of high-quality companies reported financial statements, reduce financing costs, to win the competition. This requires accountants should have high professional standards and accounting professional judgment ability to handle complex situations. Indirect impact is mainly reflected in the accounting standard improvement in China. The current IFRSs and the continuous improvement of ASBEs allows the gradual convergence of these two criteria.

(4) In the empirical part, this thesis chose 15 companies out of 95 enterprises which have been listed in the markets of both Hong Kong and mainland China to analyze

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its comparability index. The result shows that nine of them are between 0.90 and 1.10 which means the reported IFRSs net income and the reported ASBEs net income are convergent. To make up for the limits of sufficient statistics of comparability index. This thesis introduces another measurement RONA to measure a corporation's performance comparatively with that of its competitors. The results of those sample companies tend to be stable in general except for Hisense Kelon Electrical's sudden increase in 2015 and ZTE Corporation's sharp decrease in 2015, which reflect that the application of IFRSs is good to make the corporation and the entire market more stable. What's more, the issue of Interpretation No. 2 also prove that it helps improve financial reporting quality and companies' financial statements, once harmonized, became more transparent and comparable.

## **6.2 Contributions**

By conducting the precedent studies, we have made the contributions on the information concerning the convergence of IFRSs with ASBEs. Through the comparison with the prior studies, we've performed more industrial-level comparative analysis in detail and specific accounting standards. What's more, based on the listed enterprises' annual reports, we analyzed their comparability index and return on net assets. We got the result that although ASBEs have not fully converged to IFRSs, the gap between these two standards are narrowing. Adoption of IFRSs also helps Chinese

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companies operate more stable and safely. And in the Chinese financial industry, further harmonization may well be hard to obtain due to the political restrictions and the industrial characteristics in the Chinese environment. Therefore, the practices of accounting are actually keeping pace with the continuous variations and the financial and governmental context.

### **6.3 Limitations**

Based on the previous analysis, we need to take some limitations into consideration in the thesis. The main limitation relates to the sample, choice and construction of the research model. As comparing comparability index between different companies in 2015, 2016 and 2007, the selected samples do not include all the types of listed enterprises, and they are all from the financial industry, which means that it does not reflect other industries' characteristics in our thesis. And we cannot summarize the result that ASBEs and IFRSs are convergent because the lack of enough and sufficient statistics, also the time when those companies went public differ from each other.

Another limitation is the small size of the selected samples in our thesis. according to comparisons of the RONA between different companies from 2008 to 2017, the samples selected are 8 enterprises. In the year of 2007 and 2008, the number of the enterprises with the issuance of both H shares and A shares is just 30, which becomes much smaller as these enterprises are classified into the industries they represent. Hence,

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not all circumstances, which may have caused the difference between IFRSs and ASBEs, have been included in the study due to the small sample size. Additionally, the samples we chose are presented under IFRSs or HKFRSs. Since IFRSs and HKFRSs are fully converged, we consider there are no difference on RONA under these two standards.

#### **6.4 Proposal for further studies**

More rigid financial regulations have been carried out due to the current unstable economic conditions. How would it influence the current accounting standards? During the financial tsunami, the performances of Chinese corporations was comparatively well and the nationalization of numerous multinational financial firms had been finished.

Will the IASB intend to use a series of regulations to make those standards more circumspect? Will it bring about a better harmonization between IFRSs and ASBEs through narrowing the discrepancies caused by some Chinese features? All these are the topics in the future, and further researches are needed to be answered.

It is also worth conducting further studies on the auditor choosing. Since there are some limitations on sample selection, only few of the corporations were chosen to be our study objects. Due to high audit cost, firms with the issuance of A shares merely choose

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Chinese local CPA firms compared with Big 4 as auditors. After Chinese accounting system being significantly reformed, has sufficient professional training of the latest ASBE been promoted to all the local auditing companies? What are Chinese CPA firms' differences compared to the Big 4? And how will these differences impact the audit report quality?



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