

YANG'S LAW AND ZHU'S MANDATE
The Roles of Accounting in
Managing the Chinese State

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杨氏规律和朱总理指令： 会计的治国角色

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Inspirations

杨时展教授

朱镕基总理

- 天下未乱计先乱
- 天下欲治计先治
- 坚持准则
- 不做假帐

Economic Development *and* Accounting and Auditing Development

- “未有经济发达的国家而二计不发达的；
- 亦未有二计不发达的国家而经济能发达的。” – Professor Yang Shizhan (circa 1992) in an essay on establishing government accountability system in China.
- Consistent with the contemporary Western thinking that accounting is a social and institutional practice (Hopwood and Miller, 1994)

Accountability Cycle = Management Cycle



A Comparative Scorecard Leading to a Puzzle

Strictly personal evaluations	China	U.S.
Fiscal Policy	A-/B	D/F
Fiscal Management	B/C/D/F	A/B

Accounting Power: Moderate Success in the U.S.

Common American Govt. Accounting Practices

- Most govts. issue comprehensive annual reports soon after the end of fiscal year.
- Generally accepted accounting principles (GAAP) are available to evaluate quality of financial statements.
- Statements of financial position presents economic resources and long-term liabilities.
- Statement of financial performance presents costs of service, including those deferred to the future for payment.

Function (Power?) of Accounting in Relation to the Budget

- Accounting enforces the budget “as given” (e.g. for budgetary control purposes, considering contractual obligation as spending).
- Accounting provides data of actual performance in comparison with the budget:
 - Actual revenues vs. projected revenues
 - Actual spending vs. appropriations
 - Unfavorable and favorable variances as feedback to improve performance or adjust targets

Accounting Critiques Budgeting

- Often American govt. budgets project cash receipts as revenue, and make appropriations to cover cash payments – i.e. cash budgeting.
- Using the accrual basis, accounting points out the receivables and payables – both short-term and long-term.
- Accrual deficit numbers highlight “legacy costs” that burden future generations.

U.S. Government Adjusted Accrual vs. Cash Deficit

Amounts in Billions of US\$	FY 2009	FY 2008
Accrual Def.	-1,253	-1,009
Cash Def.	-1,417	-455
Difference	164	-554

Major Differences Between Cash and Accrual Deficits in Billions (FY 2008)

Liabilities for military employee benefits	110
Liabilities for veteran's compensation	339
Liabilities for civilian employee benefits	101
Depreciation expense	55
Capital expenditures	106

Accounting Provides Evidence for Auditing

- Accounting provides “audit trails” for auditing.
- Most successful for ensuring credibility of financial statements.
- Important role in ensuring compliance with finance-related laws and regulations.
- Potential role in “3E” audits of economy, efficiency and effectiveness.

An American Dilemma

- After three waves of government to
 - Ensure government officials' financial integrity
 - Support systematic, professional financial management
 - Produce much public financial information;
- American govt. acctg. has to simplify the information and interest a financially illiterate public.

Challenges in Chinese Government Accounting Reform

Lax or Even Breakdown of Basic Financial Control

- Revelations in the annual “audit storms” during the last ten days and numerous corruption cases.
- Favorable interpretations: accounting provides evidence to auditors or prosecutors.
- Unfavorable interpretation: accounting and internal control systems fail to deter and prevent malfeasance.

Inability (Reluctance?) to Account

- Current “budget accounting” system monitors cash inflows and outflows.
- The establishment of department budgets did not lead to departments accounts encompass financial resources and obligations.
- Absence of whole-government accounts of assets and liabilities – official recognition is required before measurement can take place.

Actions Outpace Regulation

- Example: Local governments are not allowed to incur deficits or to borrow.
- Reality: Many local governments incur deficits and find ways to borrow, according to observers and analysts.
- What to do?
 - Ignore what's not allowed, or
 - Acknowledge the reality and report what really has happened.

Summary: The Role of Govt. Accounting in Managing the State

- Basic role: providing data to enforce finance-related laws and regulations, including the budget.
- Intermediate role: supporting financial management of revenue and assets, expenditure and liabilities.
- Advance role: preparing financial report to demonstrate and discharge financial accountability.
- Beware of the dilemma: Will the Chinese public be more willing and able to digest the info.?

“A Seat at the Table”

Because Modern Accountants...

- In addition to keeping scores,
- Also directs managers’ attention to problem areas (e.g. cost overruns), and
- Can serve as consultant in solving financial problems to keep governments
 - Liquid
 - Solvency
 - Viable

Comments and Suggestions Welcome!

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