

CONSTRAINTS ON PROFESSIONAL SCEPTICISM IN CHINA FROM PHILOSOPHICAL AND HISTORICAL PERSPECTIVES

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Abstract- The objective of this study is to examine constraints on professional scepticism in China from historical and philosophical perspectives. Specifically, this paper examines the philosophical meanings of scepticism constructed historically in Anglo-American countries and how distinctive Chinese philosophical tradition may act as constraints on PS in China. Moreover, this paper examines how distinctive Chinese historical development of auditing may contribute to constraints on professional scepticism in China. From a philosophical perspective, the philosophical determinants of social relationships premised on conflict avoidance and obedience associated with subordination may preclude intrinsic acceptance by Chinese auditors of western notion of professional scepticism characterised with questioning, inquiry and confrontation. From a historical perspective, the alien concept of scepticism is not historically rooted in the Chinese auditing system. The analyses suggest that implementation of the alien concept of professional scepticism is likely to encounter considerable challenges in China. The findings have important implications for the international convergence of auditing standards.

Keywords: Professional scepticism, Convergence, Auditing, China.

I. INTRODUCTION

Professional scepticism (hereafter PS) is one of the most important and controversial topic in auditing. The importance of PS has been widely recognised by auditing researchers and regulators (Shaub and Lawrence 1996; Bell, Peecher et al. 2005; Nelson 2009; Hurtt 2010; Trotman 2011). PS has been regarded as “the cornerstone of audit quality” (U.K. Auditing Practices Board (APB) 2012, p.2), and “plays a fundamentally important role in the audit” (International Auditing and Assurance Standards Board (IAASB) 2012, p. 4). Recently, the fundamental importance of PS has been reiterated in the auditing standards and re-emphasised by auditing regulators worldwide.¹ Regardless of its widely recognised importance, PS remains underexplored and controversial in terms of its construct and

determinants. Particularly, very little has been known about various components embedded in the conception of PS. Nelson (2009) concludes that there is little precision in the use of the term “professional scepticism”. Consistently, Bell et al. (2005) and Hurtt (2010) urge that there is a lack of clear understanding about what constitutes PS and what are the primary indicators of its presence or absence. Furthermore, there is criticism about lack of guidance concerning implementation of the concept of PS in auditing standards (Public Oversight Board (POB) 2000; Pany and Whittington 2001). Given the importance and a lack of clear understanding of PS, there are increasing calls for more rigorous investigations concerning the construct and determinants of PS (Bell, Peecher et al. 2005), and research attention to the core issues of PS (Trotman 2011; Hurtt, Brown-Liburd et al. 2013).

Importantly, the concept of PS, stressed throughout the International Standards on Auditing (ISAs), has been diffused worldwide following the global thrust of international convergence of auditing standards. Currently, 126 countries have adopted the ISAs as issued by the IAASB (International Federation of Accountants (IFAC) 2012).² This move towards international convergence of auditing is largely driven by the assumptions based on enhancing audit quality and consistency of auditing practices throughout the world.³ However, audit quality and consistency of auditing practices may be impaired if the concept of PS is not understood in the same manner across countries. Research shows that accounting and auditing are social and institutional practices deeply embedded in the contextual environment in which it operates, rather than a neutral, objective, and value-free technical practice (Hopwood 1983; Chua 1986; Napier 1989; Gernon and Wallace 1995; Harrison and McKinnon 1999; Patel 2006; Chand, Patel et al. 2008; Hellmann, Perera et al. 2010;

¹ Internationally, IAASB staff issued Questions and Answers document: *Professional Skepticism in an Audit of Financial Statements* in February 2012 (IAASB 2012). In the U.S., Public Company Accounting Oversight Board (PCAOB) published *Staff Audit Practice Alert on Maintaining and Applying Professional Skepticism in Audits* in December 2012 (PCAOB 2012). In the U.K., Financial Reporting Council (FRC) issued discussion paper *Auditor Scepticism: Raising the Bar* in August 2010 (APB 2010) and *Professional Scepticism: Establishing a Common Understanding and Reaffirming Its Central Role in Delivering Audit Quality* in March 2012 (APB 2012). In Australia, Australian Auditing and Assurance Standards Board (AUASB) issued bulletin document: *Professional Scepticism in an Audit of a Financial Report* in August 2012 (AUASB 2012).

² The IFAC has established a number of boards to develop international standards and guidance on specific sectors of the profession, including the IAASB, the International Accounting Education Standards Board (IAESB), the International Ethics Standards Board for Accountants (IESBA), and the International Public Sector Accounting Standards Board (IPSASB) (IFAC 2011a).

³ The IAASB claims that its objective is to, “serve the public interest by setting high-quality auditing and assurance standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession” (IFAC 2011b)

Heidhues and Patel 2011). The concept of PS conceived in a predominantly Anglo-American context, has been imposed on other countries with different contexts. It is argued that particularly for emerging and transitional countries, the countries' historical, economic, political and social contexts which often differ significantly from Anglo-American countries, may result in constraints on the alien concept of PS.

The objective of this study is to examine constraints on PS in China from historical and philosophical perspectives. Specifically, this paper examines the philosophical meanings of scepticism constructed historically in Anglo-American countries and how distinctive Chinese philosophical tradition may act as constraints on PS in China. Moreover, this paper examines how distinctive Chinese historical development of auditing may contribute to constraints on PS in China. Examining PS from philosophical and historical perspectives enables us to provide insights into the contextual understanding of PS. China's unique environment, which differs significantly from Anglo-American countries, provides us an important and interesting national setting. In addition, it is worth noting that existing research on PS has primarily been conducted in Anglo-American settings. As such, the concept of PS in this strand of research has been primarily based on the Anglo-American view, which is rooted in Western philosophy and history. This view is likely to be of limited use in understanding how PS is constructed in other countries with different philosophical foundations and historical development such as China. It is therefore illuminating to obtain insights into constraints on PS in China from philosophical and historical perspectives.

The remainder of the paper is organised as follows. Section two explores origins of scepticism from the Ancient Greek philosophy and its later influences on scientific scepticism. In Section three, Chinese philosophical tradition is examined in order to identify constraints on auditors' PS from a philosophical perspective. Section four illustrates how distinctive Chinese historical development of auditing may contribute to constraints on PS in China. The last section concludes the paper with discussion and implications.

II. ORIGIN OF SCEPTICISM FROM ANCIENT GREEK PHILOSOPHY

Understanding the philosophical underpinnings of scepticism originating from the Ancient Greek may assist us to better ascertain the construction of PS conceived in Anglo-American auditing practices. The term scepticism derives from the Greek word "σκέψις" (skepsis), which means examination, inquiry into, hesitation or doubt according to the Greek-English dictionary (Liddell and Scott 1871). Accordingly, the term "sceptic", which derives from the Greek word "skeptikoi" with the original meaning of inquirers, is used to characterize those who inquiry into the truth (Landesman and Meeks 2003). In contemporary English, scepticism reflects its original meanings in Greek that focus on doubt and inquiry. According to the tenth edition of the Concise Oxford English Dictionary (Pearsall 1999), scepticism means 'doubt as to the truth of some assertion or supposed fact' and a sceptic is defined as 'a person inclined to question or doubt accepted opinions'. Given the similarity in the meanings of scepticism between the contemporary English and its Greek origination, it is

relevant and important to examine the origin of scepticism from ancient Greek Philosophy in order to provide useful insights into the adoption of the term "scepticism" in contemporary auditing practices initiated in U.S.

A. Philosophical Scepticism

The origination of scepticism can be traced back to ancient Greek philosophy where two different schools of philosophical scepticism were first formulated and endorsed, the Academic and Pyrrhonian scepticism (Lee 2010). Academic scepticism was named after Plato's Academy, and formulated by Arcesilaus (315-241 B.C.) and Carneades (213-129 B.C.) who maintained that nothing can be known for certain (Thorsrud 2010). Academics scepticism contended that it is impossible to attain knowledge, and that everything is open to doubt (Stroud 1984).

Pyrrhonian scepticism flourished as a distinct theory by Aenesidemus (100 - 40 B.C.) and was named after Pyrrho of Elis (360 - 275 B.C.) who was insisted in suspension of judgment (Svavarsson 2010). In contrast to Academics, the Pyrrhonists did not claim that knowledge is impossible, but they suspended judgment on all such theoretical questions (Svavarsson 2010). Indeed, Pyrrhonists, called themselves "Skeptikoi", meaning "inquirers", to distinguish them from those who think they have discovered the truth, and also from those who have come to the definite conclusion that the truth is undiscoverable (Bett 2010). "Skeptikoi" were regarded as those who have not closed off any options, but are still looking (Bett 2010). Pyrrhonists claimed that for any proposition asserted, the arguments supporting it are no better and no worse than the arguments against it, and hence they recommended suspending judgment (Landesman and Meeks 2003). It is the process of inducing suspension of judgment that was emphasised in characterization of Pyrrhonian scepticism (Bett 2010).

Despite various strands of scepticism running through Western philosophy, doubt about whether knowledge is attainable by human efforts is common to all versions, and they all likewise attempt to base their doubts upon rigorous arguments (Landesman and Meeks 2003, p.2). McGinn (1989, p.6) concludes that sceptics doubt the certainty of knowledge and question everything even their own judgments. Similarly, Fogelin (1994, p.3) explains that a sceptic is one who "call things into question".

B. Scientific Scepticism

Following the development of philosophical scepticism, scientific scepticism was highly influential in the development of science and the scientific method in the Seventeenth Century. Unlike philosophical scepticism which doubts the possibility of attaining any knowledge, scientific scepticism concerns ways of approaching the knowledge (even if not attaining). The major differences between philosophical and scientific scepticism is also illustrated by Bunge (1991) who suggests two distinguished scepticism: *systematic* and *methodological*. Bunge (1991) maintains that while *methodological* scepticism (equivalent to scientific scepticism) urges us to investigate, *systematic* scepticism (equivalent to philosophical scepticism) blocks research as *systematic* scepticism denies the possibility of any knowledge and therefore entails that truth is inaccessible.

Scientific scepticism is regarded as an important guiding principle in science under which it is a must to

question, doubt, or suspend judgment until sufficient information is available (Sue 1999). It plays very important role in the Empirical school of thought who emphasises the role of empirical (observed) evidence in inducing knowledge rather than deducing knowledge from innate ideas and traditions. Scientific scepticism doubts the veracity of assertions that are not supported by empirical evidence that is reproducible. It demands evidence and proof to be offered before conclusions can be drawn (Marken 1981). As a scientific methodology, scepticism is referred to as a disposition to inquiry and doubt, and the method of suspending judgment and criticism for pursuing knowledge (Kurtz 1992). Kurtz (1992, p.21-22) further summarizes: "...skepsis means 'inquiry' and 'doubt'. ... Sceptics ask, 'what do you mean?' seeking clarification and definition, and 'why do you believe what you do?' demanding reasons, evidence, justification, or proof. ..." As Kurtz (1992, p.66) concludes, "doubt initiates inquiry and leads to the formation of beliefs".

Philosophical and scientific scepticism have profound influences in the Western society. The profound influence of scepticism on the development of Western philosophy has been highly appreciated by historians of philosophy. "The sceptical philosophers and traditions are firmly located in the history of Western philosophy", and "scepticism has been a topic of central importance in modern Western philosophy and continues to excite widespread interest today" (Bett 2010, p.1). "Sceptical tradition of Western philosophy, clearly illustrate the profound influence that sceptical stances and questions have had, and continue to have, on the branch of philosophy known as epistemology, or the study of how we come to possess knowledge including whether we can possess it at all" (Landesman and Meeks 2003, p.1). It is clear that scepticism is highly appraised as a way of approaching knowledge and advance the development of science in the Western society. It is argued that the appreciation of scepticism in the Western philosophy and science is propitious to the intrinsic acceptance of PS in Anglo-American auditing practices.

Furthermore, the origins of scepticism suggest that the essence of scepticism is doubt which stimulates questioning, inquiry, criticism for searching the truth. These key elements reflected in philosophical and scientific scepticism are largely aligned with the meanings of PS illustrated by auditing regulators and researchers. For example, the ISA definition describes important elements of PS as "a questioning mind", "being alert to possible misstatements", and "a critical assessment of audit evidence" (IAASB 2010, paragraph 13, p.15). As an attitude, PS is fundamentally a sceptical mindset which drives auditors to adopt a questioning approach (IAASB 2012). Furthermore, while academic views on the meanings of scepticism vary, key elements reflected in philosophical and scientific scepticism are embraced. Shaub and Lawrence (1996, p.126) define sceptical thoughts as "willingness to doubt, question or disagree with generally accepted conclusions or clients' assertions". Also, Hurr (2010) identified six characteristics of PS including a questioning mind, suspension of judgment, searching for knowledge, interpersonal understanding, self-esteem and autonomy which are closely associated with the philosophical underpinnings of scepticism.

III. CHINESE PHILOSOPHICAL TRADITION

While scepticism originating from Greek philosophy has profound influence in Western societies, it should not be presumed that the concept of scepticism would be understood in the same way in other countries with different philosophical tradition. As such, further investigation into relevant Chinese traditional philosophy is warranted in order to understand constraints on PS in China. Specifically, insights into the Chinese traditional philosophy may be gained by examining Confucianism (*Rujia* 儒家) and Legalism (*Fajia* 法家) as they are the most influential schools of philosophy in China. Accordingly, the historical background and the key principles of these schools of philosophy are discussed in order to provide an understanding about the philosophical context in China.

A. Confucianism

Confucianism, which is derived from the teachings of the Chinese philosopher Confucius, is seen as the traditional root of Chinese culture. "Confucius is a Latinised form of the Chinese name *Kong Fuzi*, Master Kong, which is in turn a reverent title for *Kong Qiu* or *Kong Zhongni* (551 - 479 B.C.)" (Yao 2000, p.21). Confucianism is a complex system of moral, social, political, philosophical thought that has profound influences on the Chinese culture (Bond and Hwang 1986). Confucianism constitute the fundamental social values and norms that were shared within society in ancient China for over two thousand years (Yao 2000; Lin and Ho 2009). Nowadays, Confucius' thought remains powerful and influential across all Chinese societies (Yao 2000; Lin and Ho 2009). Even the current Chinese government is still promoting one of Confucius' favourite concepts, namely, *hexie* (harmony) (Higgins 2010).

The fundamental assumption of Confucianism is that an individual, as a social or relational being, exists in relation to others. A person is seen "as a relational being, socially situated and defined within an interactive context" (Bond and Hwang 1986, p. 215). Confucianism emphasises that an individual is an integrated part of the collective which he or she belongs (Bond and Hwang 1986). The fundamental assumption of interdependence is deeply embedded in the ultimate goal of familial, social and political stability and *hexie* (harmony 和谐). Confucius called for maintaining the established social order to achieve social harmony (Jacobs, Guopei et al. 1995). Confucius advocated "let the ruler be a ruler, the minister be a minister, the father be a father, and the son be a son" (Confucian Analects in Lu 1983). The focus is on people accepting a hierarchical order in which everybody has a rightful place that needs no further justification (Bond and Hwang 1986). Confucianism maintained the importance of family and "five relationships" (*wu lun* 五伦) including hierarchical relationships between father and son, husband and wife, older brother and younger brother, ruler and subject, and friend and friend.⁴ In each of the relationships, the superior member has the duty of benevolence and care for the subordinate member, and the subordinate member has the duty of obedience (Ross 2012).

⁴ In Confucianism, the relationship between friends is considered to be similar to that between brothers in which the older is superior to the younger and thus the younger should respect the older.

To maintain harmony within hierarchical relationships, Confucianism stressed the importance of obedience associated with subordination and conflict avoidance. Confucius demanded unreserved obedience of the son to his father, of the younger to the older, of the subject to the ruler (Lang 1968). In order to build an orderly society, Confucian promoted complete subordination of inferiors by expressing “love and piety towards superiors, as well as observance of rites and rules of propriety” (Lang 1968, p.9). Particularly, Confucianism emphasizes “filial piety” (*xiao* 孝), which requires “subordinations of personal desires to a hierarchy of deference that reaches up to the father, back to the ancestors, and up to heaven” (Cornberg 1994, p.138). Mencius, one of the most famous Confucian and principal interpreters, stated that “content of benevolence is the serving of one's parents; the content of dutifulness is obedience to one's elder brother” (quoted in Yearley 1975, p.189). Furthermore, harmony maintenance has been regarded as a response to conflict in the Chinese society (Leung, Brew et al. 2011). Tendency to conflict avoidance of Chinese is attributed to the emphasis of harmony in Confucianism which encourages tolerance of interpersonal disagreement (Hwang 1987).

Confucianism with the underlying assumption of interdependence, and ultimate goal of harmony within hierarchical order, emphasises the importance of complete subordination, unreserved obedience, accepting hierarchical order and conflict avoidance. Inferiors are expected to accept their social position and obey superiors without any question and in any circumstance. To avoid conflict, tolerance of disagreement rather than confrontation is the main method to deal with conflict. This may suggest that main aspects of scepticism in Anglo-American view such as inquiry and criticism would not be encouraged in Confucianism due to their confrontation features. This means the application of scepticism may not be compatible with doctrines of Confucianism. As such, in the construction of PS in China, inquiry and criticism may not be major focuses. Rather, conflict avoidance and harmonious concerns in social relationships are likely to play important roles.

B. Legalism

Legalism (*Fajia* 法家) is another important Chinese traditional philosophy which may provide useful insights into classic Chinese thought. As Cheung and Chan (2005) conclude, while Confucianism forms the principal part of Chinese culture, other philosophies such as Legalism play essential and integral roles. Indeed, Confucianism and Legalism have been regarded as the two influential political traditions which remains useful in examining social and political issues today (Bell 2009). As modern observers of Chinese politics and society have argued, Legalism has merged with mainstream Confucianism and influenced Chinese society as strongly as Confucianism (Wei 1972; Qian 1979; Sun 1992; Wei 2000).

While Legalism did not have a recognised founder, *Han Fei Tzu* (233 B.C.) is widely acknowledged as the greatest theoretical synthesizer of Legalism, whose work superseded the works attributed to his predecessors including *Shang Yang* (338 B.C.), and *Shen Pu-hai* (400 B.C.) (Hsieh 1985). Legalism became the central governing ideology of the *Qin* Dynasty (221 - 206 B.C.), the first

emperor unified China, which was regarded as a victory for the Legalists (Hsieh 1985). While unlike Confucianism, Legalism was not officially endorsed in the long history of feudal dynasties after the Qin, it was used as a tool to serve governing purpose of the ruler in feudal dynasties. Legalism has had a great impact on Chinese society particularly in political domains.

The Legalists stressed three principles of government: *Fa* (法, law), *Shu* (术, mechanism) and *Shi* (势, authority or power) to ensure that a ruler was in absolute control of his subjects (Chang 1976; Sun 1992; Wei 2000; Schneider 2011). *Fa* literally means the law, which emphasises the legal code is to be clearly written and made public. However, it covers a much larger semantic range including government scheme, institution, or even standard (Schneider 2011). *Shu* means method, tactic, or mechanism, and in a broad view is regarded as administration (Schneider 2011). It refers to the methods of control which emphasized the importance of building a punishment-and-reward system. Legalists recognized that *shu* meaning method and technique for control as an essential element for maintaining control and power (Cheng 1981). *Shi* refers to legitimacy, power and authority, which emphasises the importance of maintaining the position and leadership image of the ruler. This means hierarchical order is required to be maintained by all means to ensure the ruler's controlling position. It seems clear, however, that the well-being or the interest of the governed is not a major concern for the legalists, and is not part of their motivation for governing the state (Schneider 2011).

Legalism emphasises the importance of strict abidance by governing rules, maintenance of hierarchical order and absolute obedience by the governed. “The ruler wants absolute power over his people and thus has to establish strict and tight control. He wants to make all decisions and wants these decisions to be obeyed and carried out by his subjects” (Cheng 1981, p.276). The doctrines of Legalism require that the governed as inferiors should obey the ruler as superior. This implies that no doubt, question or criticism should be posted by the governed about the absolute power and control of the ruler. The governed should follow the implementation of *Fa*, *Shu*, and *Shi* by the ruler. Accordingly, the essence of scepticism such as doubt, questioning and criticism is absent and not encouraged in the philosophy of Legalism.

Overall, Chinese traditional philosophy centred in doctrines of Confucianism and Legalism, emphasise obedience, values of interdependence and harmony within hierarchy. It seems that the essence of scepticism promoted in Western philosophy, such as doubt, questioning and criticism, has rarely emerged in Chinese traditional philosophy. This suggests that scepticism is a western concept alien to Chinese philosophical tradition. Unlike in Anglo-American countries where scepticism is embraced in Western philosophy, there is a lack of philosophical foundation of scepticism in China. This lack of philosophical foundation of scepticism is likely to affect how auditors' PS is constructed in China. This also suggests that the Anglo-American views of the concept of PS in prior studies may not be applicable in China. Given that Chinese traditional philosophy, particularly Confucianism and Legalism, is deeply ingrained in the Chinese culture, it is important to examine how the alien concept of scepticism is

understood from these philosophical perspectives in order to enhance contextual understanding of the construction of PS in China. Without an understanding of the philosophical foundation embedded in the social interactions of Chinese auditors, it would be difficult to ascertain the construction of PS in China.

IV. HISTORICAL DEVELOPMENT OF AUDITING IN CHINA

In this section, historical development of auditing in China is examined to gain insights from a historical perspective. The value of historical understanding in accounting is significant as it enables us to place contemporary issues in a more complete perspective by understanding the elements of past accounting evolution (Previts, Parker et al. 1990). Accounting history can help us to better understand our present and to forecast or control our future (Haskins 1904). Understanding history of auditing development in China and its major features enables us to gain richer insights into the relation of such a history to present trends in auditing practices. Specifically, given that the construction of key auditing concepts, such as auditor independence and PS is embedded in auditing practices, this historical understanding of auditing helps us to provide a more complete and comprehensive insight into how these imported auditing concepts are constructed in the China's unique contexts.

A. Auditing development from ancient China to 1949

Auditing systems in China have one of the longest histories in the world (Aiken and Lu 1993b; Aiken and Lu 1998). One important feature of the auditing development in China over the long centuries of feudal dynasties is the high degree of state control (Aiken and Lu 1993b). The earliest reference to auditing in China can be traced back to the Hsia dynasty (2206–1766 BC), when concepts of accounting and auditing which incorporated accountability were introduced (Fu 1971). In the *Western Zhou* dynasty (1100–771 BC), *Zai-Fu*, a special official in charge of checking all revenues and expenditures, was introduced, which is regarded as the earliest form of auditing in China (Lau and Yang 1990). During the *Qin* dynasty (221–206 BC), “there were specific supervision rules relating to auditing of accounts, supervision and responsibility in finance and the economy” (Zhao 1987, p.173). The *Bi-Bu* system in the *Tang* Dynasty (618–907), which required the auditing function carried by *Bi-Bu* (the Auditing Department) to be separated from the Finance Ministry and placed under the direction of *Xing-Bu* (the Punishment or Justice Ministry), is regarded as one of the most important advances of auditing development (Lu and Aiken 2003). Even though the degree of responsibility and authority, and the form of audits, varied from one dynasty to another, the emphases of auditing during that time were on checking the completeness of financial records of the imperial kingdom, and the honesty of government officials in handling the money and properties of the imperial kingdom (Tang, Chow et al. 1992). During the feudal dynasties, the government, that was under the ultimate control of the emperor, played a major role in managing and regulating the feudal economy. The main objective of auditing was to serve the governing and control purpose of the emperor with respect to economic resources.

The *Opium War* (1840-1842) opened the door of China to foreign countries and turned China into a semi-feudal and

semi-colonized country (Su 1985). Since then China had experienced a turbulent period passing through late *Qing* Dynasty (1840-1911), *Warlord* government (1911-1927) and the *Nationalist* government (1927-1949). With the entrance of colonialists, the practices of public accounting were introduced into China through the operating of foreign companies in the country (Lin 1998). During this period, a series of accounting and auditing reforms largely based on foreign practices was undertaken by the government to align the financial systems with economic changes. During the time of *Warlord* (1911-1927), the government issued the first auditing law in China in 1914 which was largely based on Japanese laws, but they were never fully implemented (Lu, Ji et al. 2009). The certified public accountant (CPA) system in China first emerged in 1918 when the government issued the first regulation governing public accounting profession, the *Tentative Regulations for Accountants*, and the first public accounting firm established in Beijing (Yee 2009). This was the first appearance of a CPA profession in China. In the period of the *Nationalist* government (1927-1949), the Japanese influence was overtaken by the Anglo-Saxon influence over the auditing reforms because the Nationalist government adopted a pro-British and American policy (Lin 1998). In 1931, the Nationalist government established a new governmental financial structure under which the control of financial administration, accounting, treasury and auditing functions was assigned separately to different government departments, which are the Ministry of Finance, the Accounting Department, the Central Bank and the Auditing Department (Lu, Ji et al. 2009). Overall, during the turbulent period through the *Opium War* till the establishment of the People's Republic of China (1840-1949), auditing underwent considerable changes with impacts from various countries, and western auditing concepts and practices were initially introduced to China. The government played a leading role in the auditing reforms with emphasis on government audit. In the private sector, early development of public accounting evolved at a very slow pace with small quantity of public accountants and insignificant volume of public accounting services existing only in major cities (Lin 1998).

B. Auditing development after 1949

Since the establishment of People's Republic of China in 1949, the Communist Party has assumed the continued monopoly of political power and firmly controls the Chinese government regardless of the existence of a number of minority parties (Cheng 2008). The communist government implemented highly centralized economic planning and control imported from the Soviet Union. During the time of the centrally planned economy (1949-1978), businesses were operated and strictly controlled by government agencies and state-owned enterprises (SOEs) had an exclusively dominant role in economy (Geng, Yang et al. 2009). The primary purpose of accounting under the centrally planned economy was to serve government's planning and control needs (Winkle, Huss et al. 1994). Financial supervision was directly administrated by government agencies, such as Ministry of Finance (MOF), thus there was no need for public audit services provided by a third party (Lau and Yang 1990). Public accounting practices rooted in the private sector became unacceptable in the planned economy (Lin 1998). The entire system of

auditing, both in the private sector and the government sector, was abolished because the fully nationalised economy was under direct administration of the government (Lin 1998). The development of the auditing profession came to a halt until China's economic reform initiated in 1978 (Aiken and Lu 1998).

Following the implementation of the "open door" policy and the economic reforms initiated in 1978, China has been transformed from the centrally planned economy into a market-oriented model. The reform of the Chinese economy resulted in the increasing demand for audit services (Zhou 1988). The government decided to restore public accounting in conjunction with a restoration of the state auditing system (Lin 1998). The national auditing office (NAO) was set up in 1982 to take the lead in re-establishing state auditing systems across the country for audits of all government departments and state own enterprises (Lin 1998). The government exerted its control over public accounting through the Ministry of Finance (MOF) in issuing the *CPAs Law*, supervising CICPA and promulgating the auditing standards. The issuance of the *Provisional Regulation Concerning the Establishment of Accounting Consultancies* by the Ministry of Finance in 1980 marked the first step in the reestablishment of the CPA profession (Yee 2009). In 1981, the first CPA firm emerged as part of the revival of the certified public accountants system (Yee 2009). Since then, public accounting has undergone a remarkable growth in China. *The Regulations of Certified Public Accountants of the People's Republic of China*, was promulgated in 1986 to strengthen the government control of CPA certification and audit firms (Zhou 1988). Following the regulations which delegated the authority to CPAs to form their own professional body, the Chinese Institute of Certified Public Accountants (CICPA) was established in 1988 and placed under supervision of the MOF (Yee 2009). The enactment of the *Law of the People's Republic of China on Certified Public Accountants (CPAs Law) 1993* further provided legal foundation governing the CPA profession (Cooper, Chow et al. 2002).

Due to the constrains in capital and resources, the majority of CPA firms in China were founded and managed by government agencies, such as the finance bureau and the tax bureau (Tang 2000). In order to improve auditor independence, the MOF launched the disaffiliation programme by during 1997-1998 to disaffiliate audit firms from their sponsored government agencies (Gul, Sami et al. 2009). However, even after legal ties were cut off, the government retained significant influence over the CPA firms through its role as controlling shareholder of State Owned Enterprises, the main clientele for many audit firms (Lu, Ji et al. 2009).

Given the very recent history of public accounting in private sectors in China, the adoption of the concept of PS originating from Anglo-American public accounting practices has also been very recent. The first appearance of the term scepticism in auditing context may be traced back to the release of the US Securities and Exchange Commission (SEC) on the McKesson & Robbins case in 1940 where auditors were required to "go into an audit with a copious amount of scepticism" (AICPA 1988b, p.84). The concept of PS is formally introduced in auditing by the pronouncement of the US Statement on Auditing Standards

(SAS) No. 16⁵ in 1977 (successively superseded by SAS 53⁶ in 1988, SAS 82⁷ in 1997, and SAS 99⁸ in 2002) (Cushing 2000; Vanasco, Skousen et al. 2001). Comparably, in China it has been less than two decades since the formal introduction of PS in the first set of auditing standards in 1996 (Lin and Chan 2000).

C. Historical analysis

In the historical development of auditing in China through feudal dynasties till current market-oriented economy, two major features have been identified, including the dominate role of government and the very recent history of public auditing. These features have important implementations for understanding contemporary auditing practices and constraints on PS in China. First, given the controlling power of government over almost every aspect of the country, the state has dominated the process of auditing development from feudal society to modern China. This dominate role of government in the development of auditing has remained, despite strong foreign influences in recent history, including from Japan in the 1910s, from the Soviets in the 1950s, and from Anglo-American sphere since the 1980s. As concluded by Lu, Ji et al. (2009), government, despite different dynasties and regimes, has always dominated the development of accounting and auditing in China. During the long history through feudal society until the establishment of People's Republic of China in 1949, auditing mainly served the governing and control purpose of government. Today, the government retains significant influence over the CPA firms through its role as controlling shareholder of State Owned Enterprises, the main clientele for many audit firms (Lu, Ji et al. 2009). The history of auditing development in China shows that historically auditors mainly served the need of government control rather than act as an independent party to serve proprietary interest of external users of financial reports. Consequently, it was the role of control rather than independence that was emphasised in the auditing function. This suggests that the notion of scepticism closely associated with auditor independence is not historically rooted in the Chinese auditing system. As such, implementation of PS is likely to encounter great challenge.

Second, while the development of government auditing has rich history, the development of auditing in private sectors is very recent. Given the recent history of adopting the concept of PS, it is argued that implementing these alien auditing concepts in China is likely to encounter significant challenges. Accounting history shows that despite foreign influences, convergence with alien practices was slow in China, which may be attributable to the strong forces of historical and cultural tradition (Lu, Ji et al. 2009). Learning from the history, we can expect that it would encounter great challenge for the alien concept of PS to function properly in the Chinese auditing practices. Unlike Anglo-American auditing profession where the concept of PS originated and has been applied for a longer history, Chinese auditing

⁵ SAS No. 16: "The Independent Auditor's Responsibility for the Detection of Errors and Irregularities"

⁶ SAS 53 "The Auditors' Responsibility to Detect and Report Errors and Irregularities"

⁷ SAS 82 "Consideration of Fraud in a Financial Statement Audit"

⁸ SAS 99 "Consideration of Fraud in a Financial Statement Audit"

profession may face significant challenges profession in dealing with issues related to PS.

V. DISCUSSION AND CONCLUSION

This paper examines constraints on PS in China from historical and philosophical perspectives. Specifically, this paper examines the philosophical meanings of scepticism constructed historically in Anglo-American countries and how distinctive Chinese philosophical tradition may act as constraints on PS in China. Furthermore, this paper examines how distinctive Chinese historical development of auditing may contribute to constraints on PS in China. The analyses from historical and philosophical constraints on PS suggest that the alien concept of PS may not be readily compatible to the Chinese contexts. The philosophical determinants of social relationships premised on conflict avoidance and obedience associated with subordination may preclude intrinsic acceptance by Chinese auditors of western notion of PS characterised with questioning, inquiry and confrontation. Furthermore, the notions of independence and scepticism are not historically rooted in the Chinese auditing system. As such, implementation of the alien concept of PS is likely to encounter considerable challenges in China.

Understanding philosophical and historical constraints on PS in China has important implications for international convergence of auditing standards. Being driven by the convergence, the concept of PS conceived in a predominantly Anglo-American context, has been imposed on other countries with different contexts. However, particularly for emerging and transitional countries, the historical, economic, political and social contexts often differ significantly from Anglo-American countries. Analyses on constraints on PS from philosophical and historical perspectives suggest that contextual environment cannot be ignored in the process of the convergence. Even with the adoption of a single set of auditing standards, how these standards are constructed within a country is likely to be influenced by the country's specific contextual environment. As such, more attention needs to be given to application of these standards in its nation-specific context. Better understanding a country's specific contexts can assist us in providing advice on enhancing the international convergence that is feasible and compatible to the contextual environment.

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