# Accounting Standards for Enterprises No. 22 - Recognition and Measurement of Financial Instruments

**No. 3 [2006] of the Ministry of Finance**

Chapter I General Principles

Article 1With a view to regulating the recognition and measurement of financial instruments, the present Standards are formulated according to the Accounting Standards for Enterprises - Basic Principles .

Article 2The term "financial instruments" refers to the contracts under which the financial assets of an enterprise are formed and the financial liability or right instruments of any other entity are formed.

Article 3The term "derivative instruments" refers to the financial instruments or other contracts which are involved in the present Standards and are characterized by the following:

(1)The values thereof varies with particular interest rates, prices of financial instruments, prices of commodities, foreign exchange rates, price indexes, premium rate indexes, credit ratings, credit indexes and other similar variables; if the variable is a non-financial variable, there shall not exist any special relationship between such variable and any party to the contract;

(2)No initial net investment is required, or, as compared to contracts of other types that have similar responses to the market changes, very little initial net investment is required;

(3)It is settled on a certain future date.

Derivative instruments shall include forward contracts, futures contracts, exchanges and options, as well as the instruments that contain one or more of the characters of a forward contract, futures contract, exchange or option.

Article 4The following items shall be subject to other relevant accounting standards:

(1)The long-term equity investments as regulated by the Accounting Standards for Enterprises No. 2 - Long-term Equity Investment shall be subject to the Accounting Standards for Enterprises No. 2 - Long-term Equity Investments;

(2)The share-based payments as regulated by the Accounting Standards for Enterprises No. 11 - Share-based Payments shall be subject to the Accounting Standards for Enterprises No. 11 - Share-based Payments;

(3)The recombination of debts shall be subject to the Accounting Standards for Enterprises No. 12 - Debt Recombination;

(4)The rights available from the settlement of anticipated debts shall be subject to the Accounting Standards for Enterprises No. 13 - Contingencies;

(5)The contingent consideration contracts of the combining parties in business combinations shall be subject to the Accounting Standards for Enterprises No. 2 - Business Combination;

(6)The rights and obligations involved in a lease shall be subject to the Accounting Standards for Enterprises No. 21 - Leases;

(7)The transfer of financial assets shall be subject to the Accounting Standards for Enterprises No. 23 - Transfer of Financial Assets;

(8)Hedges shall be subject to the Accounting Standards for Enterprises No. 24 - Hedging;

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(9)The rights and obligations involved in the original insurance contracts shall be subject to the Accounting Standards for Enterprises No. 25 - Original Insurance Contracts;
(10)The rights and obligations involved in a re-insurance contract shall be subject to the Accounting Standards for Enterprises No. 26 - Re-insurance Contracts;
(11)The equity instruments as issued by an enterprise shall be subject to the Accounting Standards for Enterprises No. 37 - Presentation of Financial Instruments.
Article 5The present Standards does not regulate the irrevocable credit commitments as made by enterprises (i.e., commitments to grant loans), with the exception of the following:
(1)the designated commitments to grant loans made to the financial liabilities which are measured at their fair values, of which the variation is recorded into the profits and losses of the current period;
(2)the commitments to grant loans which can be settled with the net amount of cash or by way of exchange or by issuing any other financial instruments; and
(3)the commitments to grant loans at an interest rate which is lower than the market interest rate.
For the commitments to grant loans not regulated by the present Standards, the Accounting Standards for Enterprises No. 13 - Contingencies shall apply.
Article 6The present Standards does not regulate the contracts, which are concluded for the stipulated purchase, sale or use, and, when the time becomes mature, non-financial items are bought or sold as a performance of the contract. However, the contracts which can be settled with cash or the net amount of other financial instruments or can be bought or sold and settled by exchanging financial instruments shall be subject to the present Standards.

Chapter II Classification of Financial Assets and Financial Liabilities
Article 7Financial assets shall be classified into the following four categories when they are initially recognized:
(1)the financial assets which are measured at their fair values and the variation of which is recorded into the profits and losses of the current period, including transactional financial assets and the financial assets which are measured at their fair values and of which the variation is included in the current profits and losses;
(2)the investments which will be held to their maturity;
(3)loans and the account receivables; and
(4)financial assets available for sale.
Article 8Financial liabilities shall be classified into the following two categories when they are initially recognized:
(1)the financial liabilities which are measured at their fair values and of which the variation is included in the current profits and losses, including transactional financial liabilities and the designated financial liabilities which are measured at their fair values and of which the variation is included in the current profits and losses; and
(2)other financial liabilities.
Article 9The financial assets or liabilities meeting any of the following requirements shall be classified as transactional financial assets or financial liabilities:

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(1)The purpose to acquire the said financial assets or undertake the financial liabilities is mainly for selling or repurchase of them in the near future;
(2)Forming a part of the identifiable combination of financial instruments which are managed in a centralized way and for which there are objective evidences proving that the enterprise may manage the combination by way of short-term profit making in the near future;
(3)Being a derivative instrument, excluding the designated derivative instruments which are effective hedging instruments, or derivative instruments to financial guarantee contracts, and the derivative instruments which are connected with the equity instrument investments for which there is no quoted price in the active market, whose fair value cannot be reliably measured, and which shall be settled by delivering the said equity instruments.
Article 10Besides the provisions of Article 21 and 22 of the present Standards, only the financial assets or financial liabilities meeting any of the following requirements can be designated, when they are initially recognized, as financial assets or financial liabilities as measured at its fair value and of which the variation is included in the current profits and losses:
(1)The designation is able to eliminate or obviously reduce the discrepancies in the recognition or measurement of relevant gains or losses arisen from the different basis of measurement of the financial assets or financial liabilities;
(2)The official written documents on risk management or investment strategies of the enterprise concerned have recorded that the combination of said financial assets, the combination of said financial liabilities, or the combination of said financial assets and financial liabilities will be managed and evaluated on the basis of their fair values and be reported to the key management personnel.
The equity investment instruments, for which there is no quoted price in the active market and whose fair value cannot be reliably measured, shall not be designated as a financial asset which is measured at its fair value and of which the variation is recorded into the profits and losses of the current period.
The active market refers to the markets which are concurrently featured by the following:
(1)The objects of transaction in the market are homogeneous;
(2)Buyers and sellers are available at any time to undertake the transaction at their own free will; and
(3)The pricing information of the market is open.
Article 11The term "held-to-maturity investment" refers to a non-derivative financial asset with a fixed date of maturity, a fixed or determinable amount of repo price and which the enterprise holds for a definite purpose or the enterprise is able to hold until its maturity. The following non-derivative financial assets shall not be classified as investments held to their maturity:
(1)the designated non-derivative financial assets which, at their initial recognition, are measured at their fair values and of which the variation is included in the current profits and losses;
(2)the non-derivative financial assets which are designated as sellable at their initial recognition; and
(3)loans and account receivables.
An enterprise shall, on the balance sheet date, make an appraisal on its purpose of holding and

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ability to hold. Where there is any change, it shall be dealt with according to the present Standards.

Article 12Under any of the following circumstances, it shows that the enterprise concerned does not have a clear intention to hold the financial asset investment until its maturity:

(1)The term for holding the financial assets is not definite;

(2)It will sell the financial assets when any of the following changes: the market interest rate, the fluid demand, the substitutive investment opportunity or the investment returns ratio, the source and condition of financing, or foreign exchange risk and etc., with the exception of the sale of the financial assets which is caused by any uncontrollable and independent event which is anticipated not to repeat and is difficult to be reasonably predicted;

(3)The issuer of the financial assets can settle it with a sum which is obviously lower than the post-amortization cost;

(4)Any other circumstance which shows that the enterprise concerned does not have the clear intention to hold the financial assets until its maturity.

Article 13The post-amortization cost of a financial asset or financial liability refers to the following result after adjustment of the initially recognized amount of the financial asset or financial liability:

(1)after deducting the already paid principal;

(2)after plus or minus the accumulative amount of amortization incurred from amortizing the balance between the initially recognized amount and the amount of the maturity date by adopting the actual interest rate method; and

(3)after deducting the impairment losses that have actually incurred (only applicable to financial assets).

Article 14The actual interest rate method refers to the method by which the post-amortization costs and the interest incomes of different installments or interest expenses are calculated in light of the actual interest rates of the financial assets or financial liabilities (including a set of financial assets or financial liabilities).

The actual interest rate refers to the interest rate adopted to cash the future cash flow of a financial asset or financial liability within the predicted term of existence or within a shorter applicable term into the current carrying amount of the financial asset or financial liability.

When the actual interest rate is determined, the future cash flow shall be predicted on the basis of taking into account all the contractual provisions concerning the financial asset or financial liability (including the right to repay the loan ahead of schedule, call options, similar options and etc.), and the future credit losses shall not be taken into account.

The various fee charges, trading expenses, premiums or reduced values, etc., which are paid or collected by the parties to a financial asset or financial liability contract and which form a part of the actual interest rate, shall be taken into account in the determination of the actual interest rate.

Where the future cash flow or term of existence of a financial asset or financial liability cannot be predicted reliably, the contractual cash flow of the financial asset or financial liability for the whole term of the contract shall be taken into account.

Article 15Under any of the following circumstances, it shows that the enterprise concerned is not

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able to hold the fixed term financial asset investment until its maturity:

(1)Having no available financial resources to continuously provide funds to the financial asset investment so as to hold the financial asset investment until its maturity;

(2)Being subject to the restriction of any law or administrative regulation so that it is hard for the enterprise concerned to hold the financial asset investment until its maturity;

(3)Any other circumstance showing that the enterprise concerned is not able to hold the fixed term financial asset investment until its maturity.

Article 16Where an enterprise sells its outstanding held-to-maturity investment within the current accounting year or re-classifies it as the amount of sellable financial asset, and the such amount is considerably large as compared with the amount before such investment is sold or re-classified, the surplus of such investment shall be re-classified as a sellable financial asset which shall not be classified as a held-to-maturity investment within the current accounting year and the following two complete accounting years. However, the following circumstances shall be excluded:

(1)The date of sale or re-classification is quite near to the maturity date or the repo date of the said investment (e.g., within 3 months prior to maturity) that any change of the market interest rate will produce little impact upon the fair value of the said investment;

(2)After almost all the initial principal of the investment has been drawn back by way of repayment at fixed intervals or repayment ahead of schedule according to the provisions of the contract, the remaining part of the investment will be sold or re-classified;

(3)The sale or re-classification is caused by any independent event that the enterprise cannot control, is predicted not to occur again and is hard to be reasonably predicted. Such events mainly include:

i.The held-to-maturity investment is sold due to the serious worsening of the credit situation of the investee;

ii.The held-to-maturity investment is sold due to the fact that the relevant tax provisions have canceled the relevant policies on the pre-tax credit of interest taxes against the held-to-maturity investment or have remarkably reduced the pre-tax creditable amount;

iii.The held-to-maturity investment is sold due to any important business enterprise combination or serious disposal so as to maintain the prevailing interest risk position or maintain the prevailing credit risk policies;

iv.The held-to-maturity investment is sold due to any significant readjustment of laws or administrative regulations on the scope of permitted investment or the amount of investment of any particular investment product;

v.The held-to-maturity investment is sold due to the regulatory department’s demands for significantly enhancing the fluidity of assets or significantly enhancing the risk weight of the held-to-maturity investment in the calculation of capital adequacy ratio;

Article 17"Loans and accounts receivable" refers to the non-derivative financial assets for which there is no quoted price in the active market and of which the repo amount is fixed or determinable. An enterprise shall not classify any of the following non-derivative financial assets as a loan or account receivable:

(1)the non-derivative financial assets which are to be sold immediately or in the near future;

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(2)the non-derivative financial assets which are designated to be measured at their fair value when they are initially recognized and of which the variation is recorded into the profits and losses of the current period;
(3)the non-derivative financial assets which are designated as sellable when they are initially recognized;
(4)the non-derivative financial assets whose holder finds it hard to take back almost all of the initial investment due to any reason other than the worsening of the credit of the debtor.
The funds for securities investment and other similar funds as held by an enterprise shall not be classified as a loan or account receivable.
Article 18The "sellable financial assets" refers to the non-derivative financial assets which are designated as sellable when they are initially recognized as well as the financial assets other than those as described below:
(1)loans and accounts receivables;
(2)investments held until their maturity; and
(3)financial assets measured at their fair values and of which the variation is recorded into the profits and losses of the current period.
Article 19An enterprise shall not, after classifying a financial asset or financial liability as a financial asset or financial liability measured at its fair value and of which the variation is recorded into the profits and losses of the current period when it is initially recognized, re-classify it as any other type of financial assets or financial liabilities, nor may it re-classify any other type of financial assets or financial liabilities as a financial asset or financial liability measured at its fair value and of which the variation is recorded into the profits and losses of the current period.

Chapter III Embedded Derivative Instruments
Article 20An embedded derivative instrument shall refer to a derivative instrument which is embedded into a non-derivative instrument (namely, the principal contract) so that some or all of the cash flow of the mixed instrument changes with the change of particular interest rates, prices of the financial instrument, prices of commodities, foreign exchange rates, pricing indexes, premium rate indexes, credit ratings, credit indexes or other similar variables.
The embedded derivative instruments and the principal contract jointly form into a mixed instrument, e.g., the convertible company bonds, etc.
Article 21An enterprise may designate a mixed instrument as a financial asset or financial liability measured at its fair value and of which the variation is recorded into the profits and losses of the current period, excepting those under the following circumstances:
(1)Where the embedded derivative instrument does not significantly change the cash flow of the mixed instrument;
(2)Where the derivative instruments embedded in similar mixed instruments shall obviously not be separated from the relevant mixed instruments.
Article 22Where a mixed instrument related to an embedded derivative instrument fails to be designated as a financial asset or financial liability measured at its fair value and of which the variation is included in the current profits and losses, and it can simultaneously meet the following

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conditions, the embedded derivative instrument shall be separated from the mixed instrument and treated as an independent derivative instrument:
(1)Where there is no close relationship between it and the principal contract in terms of economic features and risks; and
(2)Where it shares the same conditions with that of the embedded derivative instrument, and the independent instrument meets the requirements of the definition of derivative instrument.
Where it is impossible to make an independent measurement when it is obtained or subsequently on the balance sheet date, the mixed instrument shall be designated entirely as a financial asset or financial liability measured at its fair value and of which the variation is included in the current profits and losses.
Article 23Where the principal contract is a financial instrument after the embedded derivative instrument is separated from the mixed instrument according to the present Standard, it shall be dealt with according to the present Standard; if the principal contract is a non-financial instrument, it shall be dealt with according to other accounting standards.
Article 24When an enterprise becomes a party to a financial instrument, it shall recognize a financial asset or financial liability.
Article 25Where a financial asset satisfies any of the following requirements, the recognition of it shall be terminated:
(1)Where the contractual rights for collecting the cash flow of the said financial asset are terminated; or
(2)Where the said financial asset has been transferred and meets the conditions for recognizing the termination of financial assets as provided for in Accounting Standards for Enterprises No. 23 - Transfer of Financial Assets.
The "termination of recognition" shall refer to the writing off the financial asset or financial liability from the account or balance sheet of the enterprise concerned.
Article 26Only when the prevailing obligations of a financial liability are relieved in all or in part may the recognition of the financial liability be terminated in all or partly.
Where an enterprise transfers any of its assets used for repaying its financial liabilities into any institution or to establish a trust, and the prevailing obligations to repay the liabilities remain to exist, it shall not terminate the recognition of the said financial liability and the transferred asset.
Article 27Where an enterprise (debtor) enters into an agreement with a creditor so as to substitute the existing financial liabilities by way of any new financial liability, and if the contractual stipulations regarding the new financial liability is substantially different from that regarding the existing financial liability, it shall terminate the recognition of the existing financial liability, and shall at the same time recognize the new financial liability.
Where an enterprise makes substantial revisions to some or all of the contractual stipulations of the existing financial liability, it shall terminated the recognition of the existing financial liability or part of it, and at the same time recognize the financial liability after revising the contractual stipulations as a new financial liability.
Article 28Where the recognition of a financial liability is totally or partially terminated, the enterprise concerned shall include into the profits and losses of the current period the gap between

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the carrying amount which has been terminated from recognition and the considerations it has paid (including the non-cash assets it has transferred out and the new financial liabilities it has assumed).

Article 29Where an enterprise buys back part of its financial liabilities, it shall distribute, on the repo day, the carrying amount of the whole financial liabilities in light of the comparatively fair value of the part that continues to be recognized and the part whose recognition has already been terminated.

The gap between the carrying amount which is distributed to the part whose recognition has terminated and the considerations it has paid (including the non-cash assets it has transferred out and the new financial liabilities it has assumed) shall be recorded into the profits and losses of the current period.

Chapter V Measurement of Financial Instruments

Article 30The financial assets and financial liabilities initially recognized by an enterprise shall be measured at their fair values.

For the financial assets and liabilities measured at their fair values and of which the variation is recorded into the profits and losses of the current period, the transaction expenses thereof shall be directly recorded into the profits and losses of the current period;

for other categories of financial assets and financial liabilities, the transaction expenses thereof shall be included into the initially recognized amount.

Article 31The "transaction expenses" refers to the newly added external expenses attributable to the purchase, distribution or disposal of a financial instrument.

The newly added external expenses refer to the expenses that will occur only when the enterprise concerned purchases, distributes, or disposes of any financial instrument.

The transaction expenses include handing charges and commissions as well as other necessary expenditures an enterprise pays to its agency institutions, consultation companies, securities dealers and etc., but exclude the bond premiums, reduced values, financing expenses, internal management costs, and other expenses that are not directly related to the transaction.

Article 32An enterprise shall make subsequent measurement on its financial assets according to their fair values, and may not deduct the transaction expenses that may occur when it disposes of the said financial asset in the future. However, those under the following circumstances shall be excluded:

(1)The investments held until their maturity, loans and accounts receivable shall be measured on the basis of the post-amortization costs by adopting the actual interest rate method;

(2)The equity instrument investments for which there is no quotation in the active market and whose fair value cannot be measured reliably, and the derivative financial assets which are connected with the said equity instrument and must be settled by delivering the said equity instrument shall be measured on the basis of their costs.

Article 33An enterprise shall make subsequent measurement on its financial liabilities on the basis of the post-amortization costs by adopting the actual interest rate method, with the exception of those under the following circumstances:

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(1)For the financial liabilities measured at their fair values and of which the variation is recorded into the profits and losses of the current period, they shall be measured at their fair values, and none of the transaction expenses may be deducted, which may occur when the financial liabilities are settled in the future;

(2)For the derivative financial liabilities, which are connected to the equity instrument for which there is no quotation in the active market and whose fair value cannot be reliably measured, and which must be settled by delivering the equity instrument, they shall be measured on the basis of their costs.

(3)For the financial guarantee contracts which are not designated as a financial liability measured at its fair value and the variation thereof is recorded into the profits and losses of the current period, and for the commitments to grant loans which are not designated to be measured at the fair value and of which the variation is recorded into the profits and losses of the current period and which will enjoy an interest rate lower than that of the market, a subsequent measurement shall be made after they are initially recognized according to the higher one of the following:

i.the amount as determined according to the Accounting Standards for Enterprises No. 13 - Contingencies; or

ii.the surplus after accumulative amortization as determined according to the principles of the Accounting Standards for Enterprises No. 14 - Revenues is subtracted from the initially recognized amount.

Article 34Where an enterprise has the intention of holding or the ability to make changes so that an investment is no longer suitable to be classified as a held-to-maturity investment, the investment shall be re-classified as a sellable financial asset, and a subsequent measurement shall be made at it fair value.

The balance between the carrying amount of the said investment at the re-classification day and the fair value shall be computed into the owner’s equity, and when the said sellable financial asset is impaired or transferred out when it is terminated from recognizing, it shall be recorded into the profits and losses of the current period.

Article 35Where part of the held-to-maturity investment is sold or the re-classified amount thereof is considerably large, and if it does not fall within any of the exceptions as described in Article 16, so that the remainder of the said investment is no longer suitable to be classified as a held-to-maturity investment, the enterprise shall re-classify the remainder of the said investment as a sellable financial asset, and shall make subsequent measurement on it according to its fair value.

The gap between the carrying amount of the said remnant part of the investment at the re-classification day and the fair value shall be computed into the owner’s equity. And when the said sellable financial asset is impaired or transferred out when it is terminated from recognition, it shall be recorded into the profits and losses of the current period.

Article 36As for the financial assets and financial liabilities, which, according to the present Accounting Standards, shall be measured at their fair values, but of which the prior fair values cannot be measured reliably, the enterprise shall measure them at their fair values when their fair values can be reliably measured, and the gap between the relevant carrying amount and the fair

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value shall be dealt with according to Article 38 of the present Accounting Standards herein.

Article 37Where the intention of holding or the ability to hold changes, or the fair value can not be reliably measured any more, or the term of holding has exceeded "two complete accounting years" as described in Article 16 of the present Accounting Standards herein, which makes it no longer suitable to measure the financial asset or financial liability at its fair value, the enterprise concerned may measure the said financial asset or financial liability on the basis of its cost or post-amortization cost. And such cost or post-amortization cost at the re-classification day shall be the fair value or carrying amount of the financial asset or financial liability.

The gains or losses that are related to the said financial asset and that are directly included in the owner’ s equity shall be dealt with according to the following provisions:

(1)Where such financial asset has a fixed date of maturity, it shall be amortized within the remaining period of the said financial asset by adopting the actual interest rate method and be recorded into the profits and losses of the current period.

The gap between the post-amortization cost of the financial asset and the amount on the maturity date shall also be amortized within the remaining period of the said financial asset by adopting the actual interest rate method and be recorded into the profits and losses of the current period.

If, during the subsequent accounting period, the financial asset is impaired, the relevant profits and losses that were included in the owner’ s equity shall be transferred out and be recorded into the current profits and losses .

(2)Where such financial asset does not have a fixed date of maturity, it shall remain in the owner’ s equity. And when the said financial asset is transferred out at its disposal, it shall be recorded into the profits and losses of the current period.

Where such financial asset is impaired during the remaining period of accounting that follows, the relevant profits and losses that were included in the owner’ s equity shall be transferred out and be recorded into the profits and losses of the current period.

Article 38The profits and losses arising from the change in the fair value of a financial asset or financial liability shall be dealt with according to the following provisions, unless it is related to hedging:

(1)The profits and losses, arising from the change in the fair value of the financial asset or financial liability which is measured at its fair value and of which the variation is recorded into the profits and losses of the current period, shall be recorded into the profits and losses of the current period;

(2)The profits and losses arising from the change in the fair value of a sellable financial asset shall be included directly in the owner’ s equity with the exception of impairment losses and the gap arising from foreign exchange conversion of cash financial assets in any foreign currency, and when the said financial asset is stopped from recognition and is transferred out, it shall be recorded into the profits and losses of the current period.

The gap arising from the foreign exchange conversion of a sellable cash financial asset in any foreign currency shall be recorded into the profits and losses of the current period.

The interests of the sellable financial assets calculated according to the actual interest rate method shall be recorded into the profits and losses of the current period. The cash dividends of the

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sellable equity instrument investments shall be recorded into the profits and losses of the current period when the investee announces the distribution of dividends.
The treatment of the profits and losses arising from the change in the fair value of a financial asset or financial liability related to hedging shall be subject to the Accounting Standard for Enterprises No. 24 - Hedging.
Article 39For the financial assets and financial liabilities measured at the post-amortization costs, the profits and losses that arise when such financial assets or financial liabilities are terminated from recognition, or are impaired or amortized, shall be recorded into the profits and losses of the current period.
However, if a financial asset or financial liability is designated as an item of hedging, the treatment of the relevant profits and losses shall be subject to the Accounting Standard for Enterprises No. 24 - Hedging.

Chapter VI Impairment of Financial Assets
Article 40An enterprise shall carry out an inspection, on the balance sheet day, on the carrying amount of the financial assets other than those measured at their fair values and of which the variation is recorded into the profits and losses of the current period. Where there is any objective evidence proving that such financial asset has been impaired, an impairment provision shall be made.
Article 41The expression "objective evidence proving that the financial asset has been impaired" refers to the actually incurred events which, after the financial asset is initially recognized, have an impact on the predicted future cash flow of the said financial asset that can be reliably measured by the enterprise.
The objective evidences that can prove the impairment of a financial asset shall include:
(1)A serious financial difficulty occurs to the issuer or debtor;
(2)The debtor breaches any of the contractual stipulations, for example, fails to pay or delays the payment of interests or the principal, etc.;
(3)The creditor makes any concession to the debtor which is in financial difficulties due to economic or legal factors, etc.;
(4)The debtor will probably become bankrupt or carry out other financial reorganizations;
(5)The financial asset can no longer continue to be traded in the active market due to serious financial difficulties of the issuer;
(6)It is impossible to identify whether the cash flow of a certain asset within a certain combination of financial assets has decreased or not. But after making an overall appraisal according to the public data available, it is found that the predicted future cash flow of the said combination of financial assets has indeed decreased since it was initially recognized and such decrease can be measured, for example, the ability of the debtor of the said combination of financial assets worsens gradually, the unemployment rate of the country or region where the debtor is situated increases, the prices of the region where the guaranty is situated are obviously dropping, or the industrial sector concerned is in slump, etc.;
(7)Any seriously disadvantageous change has occurred to technical, market, economic or legal

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environment, etc. wherein the debtor operates its business, which makes the investor of an equity instrument unable to take back its investment;
(8)Where the fair value of the equity instrument investment drops significantly or not contemporarily;
(9)Other objective evidences showing the impairment of the financial asset.
Article 42Where a financial asset measured on the basis of post-amortization costs is impaired, the carrying amount of the said financial asset shall be written down to the current value of the predicted future cash flow (excluding the loss of future credits not yet occurred), and the amount as written down shall be recognized as loss of the impairment of the asset and shall be recorded into the profits and losses of the current period.
The current value of the predicted future cash flow shall be determined according to the capitalization of the original actual interest rate of the said financial asset, taking into account the value of the relevant guarantee (but the expenses arising from the acquisition or sale of the guarantee shall be deducted).
The original actual interest rate is the actual interest rate as determined when the financial asset was initially recognized. With regard to the floating interest rate loans, accounts receivable, and the investments held until their maturity, the current actual interest rate as stipulated in the contract shall be adopted as the capitalization rate in the calculation of current value of the cash flow.
Where there is a very small gap between the predicted future cash flow of a short-term account receivable item and the current value thereof, the predicted future cash flow is not required to be capitalized when determining the relevant impairment-related losses.
Article 43An impairment test shall be made on the financial assets with significant single amounts. If any objective evidence shows that it has been impaired, the impairment-related losses shall be recognized and shall be recorded into the profits and losses of the current period.
With regard to the financial assets with insignificant single amounts, an independent impairment test may be carried out, or they may be included in a combination of financial assets with similar credit risk features so as to carry out an impairment-related test.
Where, upon independent test, the financial asset (including those financial assets with significant single amounts and those with insignificant amounts) has not been impaired, it shall be included in a combination of financial assets with similar risk features so as to conduct another impairment test.
The financial assets which have suffered from an impairment loss in any single amount shall not be included in any combination of financial assets with similar risk features for any impairment test.
Article 44Where any financial asset measured on the basis of post-amortization costs is recognized as having suffered from any impairment loss, if there is any objective evidence proving that the value of the said financial asset has been restored, and it is objectively related to the events that occur after such loss is recognized (e.g., the credit rating of the debtor has been elevated, etc.), the impairment-related losses as originally recognized shall be reversed and be recorded into the profits and losses of the current period.
However, the reversed carrying amount shall not be any more than the post-amortization costs of

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the said financial asset on the day of reverse under the assumption that no provision is made for the impairment.

Article 45Where an equity instrument investment for which there is no quoted price in the active market and whose fair value cannot be reliably measured, or a derivative financial asset which is connected with the equity instrument and which must be settled by delivering the equity instrument, suffers from any impairment, the gap between the carrying amount of the equity instrument investment or the derivative financial asset and the current value of the future cash flow of similar financial assets capitalized according to the returns ratio of the market at the same time shall be recognized as impairment-related losses and be recorded into the profits and losses of the current period.

Article 46Where a sellable financial asset is impaired, even if the recognition of the financial asset has not been terminated, the accumulative losses arising from the decrease of the fair value of the owner's equity which was directly included shall be transferred out and recorded into the profits and losses of the current period.

The accumulative losses that are transferred out shall be the balance obtained from the initially obtained costs of the sold financial asset after deducting the principals as taken back, the current fair value and the impairment-related losses as was recorded into the profits and losses of the current period.

Article 47As for the sellable debt instruments whose impairment-related losses have been recognized, if, within the accounting period thereafter, the fair value has risen and are objectively related to the subsequent events that occur after the originally impairment-related losses were recognized, the originally recognized impairment-related losses shall be reversed and be recorded into the profits and losses of the current period.

Article 48The impairment-related losses incurred to a sellable equity instrument investment shall not be reversed through profits and losses.

However, the impairment-related losses incurred to an equity instrument investment for which there is no quoted price in the active market and whose fair value cannot be reliably measured, or incurred to a derivative financial asset which is connected with the said equity instrument and which shall be settled by delivering the said equity instrument, may not be reversed.

Article 49After an impairment of a financial asset, the interest incomes shall be recognized at the interest rate which is used as the capitalization rate in the capitalization of the future cash flow when the impairment-related losses are determined.

## Chapter VII Determination of the Fair Value

Article 50The "fair value" refers to the amount, at which both parties to a transaction who are familiar with the condition exchange their assets or clear off their debts under fair conditions.

In a fair transaction, both parties to it shall be enterprises in continuous operation, and do not plan or do not need to carry out any liquidation, significantly reduce their operational scale or carry out transactions notwithstanding the unfavorable conditions they face.

Article 51As for the financial assets or financial liabilities for which there is an active market, the quoted prices in the active market shall be used to determine the fair values thereof.

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The quoted prices in the active market refer to the prices, which are easily available from the stock exchanges, brokers, industry associations, pricing service institutions and etc. at a fixed term, and which represent the prices at which actually occurred market transactions are made under fair conditions.

(1)In the active market, the quoted prices of an enterprise for the financial assets it holds or the financial liabilities it plans to assume shall be the present actual offer, while the quoted prices of an enterprise for the financial assets it plans to acquire or the financial liabilities it has assumed shall be the available charge.

(2)Where an enterprise holds the assets or liabilities that can be used to counteract the market risks, it may adopt the middle price of the market to determine the fair value of the positions that can counteract the risks of the market; meanwhile, the offer or charge shall be the basis for determining the fair value of net exposure.

(3)Where there is no available offer or charge for a financial asset or financial liability, but there is no any significant change to the economic environment after the latest transaction day, the enterprise shall adopt the market quoted price of the latest transaction to determine the fair value of the said financial asset or financial liability.

Where there is any significant change to the economic environment after the latest transaction day, the enterprise concerned shall adjust its market quoted price of the latest transaction by referring to the available prices or interest rates of similar financial assets or financial liabilities so as to determine the fair value of the said financial asset or financial liability.

Where the enterprise has adequate evidences to prove that the market quoted price of the latest transaction is not a fair value, it shall make appropriate adjustment to the market quoted price of the latest transaction so as to determine the fair value of the said financial asset or financial liability.

(4)The fair value of a combination of financial instruments shall be determined according to both the number of the single financial instruments within the combination and the unit quoted price of the market.

(5)The fair value of a current deposit shall not be lower than the amount the depositor shall pay when it becomes drawable. The fair value of a deposit at notice shall not be lower than the current value of the payable amount as of the first day it becomes drawable upon the request of the depositor for draw.

Article 52Where there is no active market for a financial instrument, the enterprise concerned shall adopt value appraisal techniques to determine its fair value.

The result obtained by adopting value appraisal techniques shall be able to reflect the transaction prices that may be adopted in fair dealings on the value appraisal day.

The value appraisal techniques mainly include the prices adopted by the parties, who are familiar with the condition, in the latest market transaction upon their own free will, the current fair value obtained by referring to other financial instruments of the same essential nature, the cash flow capitalization method and the option pricing model, etc.

To determine the fair value of a financial asset, an enterprise shall choose those value appraisal techniques which are generally acknowledged by market participants and have been proved as

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reliable by past actual transaction prices of the market:

(1)To determine the fair value of a financial asset by adopting value appraisal techniques, one shall adopt, if possible, all the market parameters that are taken into account by market participants in pricing financial instruments, including the risk-free interest rates, credit risks, foreign exchange rates, commodity prices, stock prices or stock indexes, the future fluctuation rate of financial instrument prices, risks of repayment ahead of schedule, the service costs of financial assets or financial liabilities, etc., and try its best to avoid adopting those parameters that relate to particular enterprises.

(2)An enterprise shall regularly use the open transaction prices of the financial instruments that have never been revised or reorganized to rectify the value appraisal techniques it employs, and test the effectiveness of the said value appraisal techniques.

(3)The transaction price of a financial instrument shall be the best evidence for initially recognizing the fair value thereof. However, where there is any objective evidence showing that it is more fair to adopt the open transaction price of identical financial instrument or it is more fair to adopt the result determined by employing the value appraisal techniques that only take open market parameters into account, it shall not take the transaction price as the fair value for its initial recognition. Instead, it shall employ a more fair transaction price or the value appraisal result to determine the fair value.

Article 53As for the financial assets initially obtained or produced at source and the financial liabilities assumed, the fair value thereof shall be determined on the basis of the transaction price of the market.

The fair value of a liability instrument shall be determined on the basis of the market situation of the day when it is acquired or issued and the current market situation, or the current market interest rates of other similar liability instruments (namely, having a similar remaining period, mode of cash flow, pricing currency, credit risks, basis of guarantee and interest rate, etc.).

Where the credit risks of the debtor and the applicable credit risk agios remain unchanged after the issuance of the liability instrument, the benchmark interest rate may be adopted to estimate the interest rate of the current market so as to determine the fair value of the liability instrument.

If the credit risks of the debtor and the corresponding risk agios have undergone any change after the issuance of the liability instrument, the current prices or interest rates of similar liability instruments shall be referred to and the adjustment to the differences between different financial instruments shall be taken into consideration in the determination of the fair value of the liability instrument.

Article 54Where an enterprise adopts the method of future cash flow capitalization to determine the fair value of a financial instrument, it shall use the market returns ratio of other financial instruments with essentially the same contractual stipulations and features as the rate of capitalization.

The stipulations and features of a financial instrument shall include the credit quality of the financial instrument itself, the remaining period for calculating the interest at a fixed interest rate as described in the contract, the remaining period for repaying the principal, and the currency used at the time of payment and etc.

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Where there is little difference between the current value of the short-term accounts receivable and accounts payable whose interest rate has not been indicated and the actual transaction price, it may be measured at the actual transaction price.

Article 55As for the equity instrument investments for which there is no quoted price in the active market and the derivative instruments which are connected with the said equity instrument and shall be settled by delivering the said equity instrument, the satisfaction of any of the following circumstances will mean that the fair value thereof can be reliably measured:

(1)Where there is a very small range for the variation of the reasonable fair value estimate of the said financial instrument;

(2)Where, within the range of variation of the said financial instrument, the various probabilities adopted to determine the estimate of the fair values thereof can be reasonably determined.

Chapter VIII Definition of Financial Assets, Financial Liabilities and Equity Instruments

Article 56The "financial assets" refers to the following assets of an enterprise:

(1)cash;

(2)the equity instruments of other entities it holds;

(3)the cash it charged from other entities or the contractual rights to other financial assets it holds;

(4)the contractual rights it has obtained through the exchange of financial assets or financial liabilities with other entities under potentially favorable conditions;

(5)the contractual rights to non-derivative instruments which must be settled or may be settled by the enterprise with its own equity instruments in the future, whereby the enterprise will receive an unfixed amount of equity instruments of its own according to the said contract;

(6)the contractual rights to non-derivative instruments which must be settled or may be settled by the enterprise with its own equity instruments in the future, excluding the contractual rights to the derivative instruments for which the enterprise will exchange for a fixed amount of its own equity instruments with a fixed amount of cash or any other financial assets.

Particularly, the enterprise’s own equity instruments shall not include the contracts which are the basis for the enterprise to charge or pay the equity instruments of its own.

Article 57The "financial liabilities" refers to the following liabilities of an enterprise:

(1)the contractual obligations to deliver cash or other financial assets to any other entity;

(2)the contractual obligations to exchange with other entity financial assets or financial liabilities under potentially unfavorable conditions;

(3)the contractual obligations to non-derivative instruments which must be settled or may be settled by the enterprise with its own equity instruments in the future, whereby the enterprise will deliver an unfixed amount of equity instruments of its own according to the said contract;

(4)the contractual obligations to non-derivative instruments which must be settled or may be settled by the enterprise with its own equity instruments in the future, excluding the contractual obligations to the derivative instruments for which the enterprise will exchange for a fixed amount of its own equity instruments with a fixed amount of cash or any other financial assets. Particularly, the enterprise’s own equity instruments shall not include the contracts that are the

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basis for the enterprise to charge or pay the equity instruments of its own.

Article 58The "equity instruments" refers to the contracts which can prove that a certain enterprise holds the surplus equities of the assets after the deduction of all the debts.

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