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Annual Accounts

José Antonio Segarra
Jordi Carrillo

This technical note addresses the legal obligation of every corporation's management to prepare its annual accounts, which must then be submitted for approval at the general assembly of shareholders and subsequently filed for recording in the Commercial Registry. The timely and proper preparation of the company's annual accounts is one of the main responsibilities of a company's management, and derives from:

a) The manager's legal obligation to keep organized and detailed books of account, thereby demonstrating the company's long-term prospects.

b) The need for interested third parties, such as financing providers and institutions, to have reliable information in deciding to extend credit to the company.

c) The public's interest in being aware of the state of commercial businesses.

The legal framework for regulating the annual accounts is found in the Commercial Code and the Companies Act. Their preparation must be in accordance with the General Accounting Plan. Annual accounts regulations are found in Law 1/2010 on Companies.

The law imposes various record-keeping obligations for management: the inventory book, the general journal and the annual accounts.[1]

The annual accounts must follow the legally established structure and content requirements. It is mandatory to follow the established model and draft the accounts with clarity, showing an accurate view of the company's assets, financial position and performance.

[1] There are others, such as the book of members, the book of contracts between the single member and the company, the minutes book, etc.

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The documentation's structure cannot change from one year to another in order to facilitate quantitative comparisons between years, though exceptions to this general rule may be granted in extraordinary cases and with the justification provided in the supplementary information report.

Although the annual accounts ordinarily comprise the accounting of transactions from the first to the last days of a calendar year, other dates may be chosen for the start and close, provided the term is for one calendar year.

Components of the Annual Accounts

The annual accounts are composed of five documents.

According to Article 254 the Companies Act:

> "The annual accounts shall comprise the balance sheet, profit and loss statement, consolidated annual statement of changes in equity, cash flow statement and supplementary information report."

Balance Sheet

The general norms for its preparation are found in the Commercial Code, specifically in the General Accounting Plan.

Major difficulties arising in distinguishing between *current* and *non-current assets* and in distinguishing between net assets and those of other creditors (current and non-current liabilities) must be anticipated.

As general rules:

Offsetting between assets and liabilities is prohibited.

Items may be grouped if doing so will enable a clearer and more accurate view of the company.

An item of no value may be deleted, provided its non-appearance in the company's previous years.

The law provides for the option, but not obligation, to submit an abridged balance sheet, provided the company meets two of the following three requirements:

a) The total amount of items classified as assets does not exceed €2,850,000.

b) Net revenue does not exceed €5,700,000.

c) The average number of employees throughout the year does not exceed 50.

Companies submitting abridged balance sheets also face fewer formal requirements, may submit abridged versions of the consolidated statement of changes in equity and supplementary information report, and are exempt from filing a management report, cash flow statement and audit report.

The company will lose this option if it does not satisfy the requirements for two consecutive financial years.

There are various specific rules for preparing the balance sheet:

1. Each financial year's opening balance must match the preceding financial year's closing balance.
2. It must contain the numbers for the given financial year, as well as those for the immediately preceding year.
3. It may divide items and create new items not provided for by law.
4. Items may be grouped if this will provide an accurate view of the company.

Profit and Loss Statement

This statement shows the company's financial performance for the financial year. It must include revenues and expenses separately and show the difference between the two: the bottom line.

As with the balance sheet, an abridged profit and loss (P&L) statement may be submitted, provided the company meets two of the following three requirements:

a) The total amount of items classified as assets does not exceed €11,400,000.

b) Net revenue is below €22,800,000.

c) The average number of employees throughout the year does not exceed 250.

As in the case of the balance sheet, the company will lose this option if it does not satisfy the requirements for two consecutive financial years.

Consolidated Annual Statement of Changes in Equity

The importance of this document derives from the creditors' interest in knowing the changes that have occurred in the company's equity, given the implications that these have on the guarantees the creditors received in exchange for their credit.

In addition to showing all changes in the company and its partners, it also details any revenues and expenses from the year that do not factor into net income, but which do increase or diminish the company's equity.

Cash Flow Statement

Introduced in the last accounting reform, the cash flow statement organizes and groups the various categories of cash receipts and payments made by the company, thereby showing the company's cash flows for the financial year.

"Cash" is taken to be any funds deposited in the company's checking, savings or deposit accounts or any other financial instruments convertible to cash.

The cash flow statement classifies movements depending on whether they pertain to operating, investing or financing activities.