

## Miscellaneous

### The Informative Dimension of the Annex to the Annual Financial Statements in the Context of the 4<sup>th</sup> European Directive

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**Abstract:** The fundamental disposition of the CEE 4th Directive is represented by the art.2, in which is stipulated the structuring of the annual accounts in three documents that forms a unitary whole as following: the balance sheet, the profit and loss account and the annex. The annex is a constitutive part of the annual accounts, being a conceptual product mentioned in the art.2 of the CEE 4th Directive. This synthetic accounting has the role to explain or to complete the elements offered by the balance sheet and the profit and loss account. The annex represents a valuable instrument of informing and analysis for all the users of accounting information. The informative dimension of the annex is not limited, but the information presentation must respect the principle of true and fair view and that of the significant importance.

**Keywords:** the 4<sup>th</sup> European directive, annual accounts, financial statements, true and fair view, synthetic accounting documents.

**Jel Classification:** F15, F36

A dimension of the international accounting standardization is the process of accounting harmonization taking place within the European Union.

This process, initiated in the '70, targets especially the harmonization of the member states' accounting systems, in this sense being elaborated directives that must be incorporated in the national legislation of each of the member states.

The 4th Directive, elaborated in the 25<sup>th</sup> of July 1978 and revised in 1990, targets especially the coordination of the national dispositions regarding the structure and content of the annual accounts, of the administrative report, the patrimonial elements' evaluation norms, as well as the publishing of these documents for the companies on capitals (joint stock companies and limited liability companies), those having the obligation to integrate in the national legislation stipulations regarding the applicability of this directive.

This document fortifies the authorization of the accounting principles by the adoption of a legal rule (norm), referring only to the annual accounts and not to the organizing of the accounting or to the chart of accounts.

Having for source the communitarian law, the directive is compulsory for all the European Union member states and its application brings along an entire legislative procedure, having for effect the development of accounting normalization in these countries. **The juridical characteristics of the 4<sup>th</sup> Directive**, formulated in consensus with our opinion:

- Represents an unilateral act of the communitarian authority;
- Is meant for all the member states;
- Defines a result that must be achieved;
- Establishes the competence of member states, regarding the form and the means, proposing at the same time a procedure of integration in the national legislations.

The basic disposition of the Directive is concentrated in the Anglo-Saxon notion of *true and fair view*, respectively the obligation imposed to the annual accounts to offer a true image of the patrimony, financial statements and the company's results; therefore, compulsory schemes were included regarding the elaboration of the balance sheet and of the profit and loss account but also the minimal informational content of the Annex and Administration Report.

We must however point out that **the Directive is not a law** for the companies interested, but leaves a large number of options and dispositions at the service of the member states that begin with the expression „**the member states will be able to authorize**”.

This document also tries to find ways to diminish the differences concerning the structure and format of the synthetic annual documents in the conditions of more options are stipulated to be legislated by international accounting norms.

The list of options is long enough, and, in our opinion, it is possible to appear the disadvantage that certain dispositions of the Directive to be interpreted differently by the member states and the translations, in various languages, have not strictly the same significance in each and every country.

We consider that technically **the harmonization of the annual accounts signifies the approaching of their aspects: the presentation, the informing the dispositions regarding the accounting principles.**

If the two first aspects are easily into a harmony with each other, we cannot say the same about the harmonization of the accounting principles because there is no

theoretical agreement yet at the level of country, a problem still in debate even in the present.

The fundamental disposition of the whole CEE 4th Directive is represented by the art. 2, in which is stipulated the structuring of the annual accounts in three documents, that forms a unitary whole as follows:

- the balance sheet;
- the profit and loss account;
- the annex.

In the article 1, the Directive points out that its stipulations are applied to all the public limited company, Limited Liability Company and its equivalents.

The only derogations admitted are referring to the **presentation, publishing and control of the accounts** based on the criterion of the enterprise's dimensions.

This directive, as document, is made out of 61 articles, grouped in 12 sections, from which **Section nr.8**, titled "*Notes to the annual accounts*", mentions the minimal information the annex must give as synthetic accounting document.

The contents of the Directive are shared in **four parts**:

- the scheme of the balance sheet;
- the scheme of the profit and loss account;
- the evaluation norms;
- the annex to the balance sheet;
- the administrative report.

The globalization and the insufficiency of the information given by the balance sheet and the profit and loss account do not permit the achievement of the enterprise's true and fair view of the patrimony, financial situation and result. For this reason the existence of the annex as synthetic accounting document is an **informational necessity**.

The position of the annex within the assembly of the synthetic documents has generated many opinions in the specialized literature.

For some authors, „*the annex is a constitutive part of the financial statements*” (Ristea M., 2006) for others, **the annex represents an analytical approach in the conditions in which the balance sheet and the profit and loss account represent authentic synthetic documents.**

But, we subscribe to the opinion that considers “*The annex is a conceptual product, its presence being the consequence of the putting in practice of the accounting*

*principles, especially the principle of the true and fair view and the principle of the significant importance (or the significance threshold)”. (Doinea, 2005)*

The elaboration of an annex of quality means to select the information of significant importance **either for explaining or completing the elements offered by the balance sheet and the profit and loss account.**

Within the financial statements assembly, as the opinion unanimously accepted by the specialized literature states that **the annex has a double role:**

1. An **explicative role**, because it allows a better understanding of the balance sheet and the profit and loss account;
2. The **role of complementary instrument** to the balance sheet and the profit and loss account.

In this context, **certain characteristics** can be attributed to this statement:

- **The annex is a complementary document** to the balance sheet and the results' account.
- **The annex explains and comments** the information given by the balance sheet and the profit and loss account;
- **The annex includes a type list of accounting information**, information representing its **standardized contents**, that varies from one country to another, depending on the accounting tradition and the economic, juridical, social and fiscal environment specific to each country;
- **The annex is an open accounting document** because it includes any information that might contribute to the reflection of the entity's reality, respectively to offer an accurate image of the entity's patrimony, financial statement and result;
- **The annex contains only information of significant importance**, implicitly or explicitly sanctioning this notion;
- **The annex is a heterogeneous product**, being partially accountably but also extra accounting since a part of the information is extract directly from the accounts and others are taken from the entity's statistics.

In order to be useful, the annex must not be schematic, but neither an informational encyclopaedia, being necessary for furnishing only the information of significant importance to the users.

Considering the information mentioned above, in our opinion, **the annex represents a valuable informing and analyzing instrument for all the users of accounting information, since it brings clarifications to the policies promoted by the entity in the domains of investments, financing, fiscal and patrimony's evaluation.**

In the communitarian accounting law, The 4<sup>th</sup> Directive underlines „*the importance of the annex by the fact that it offers the explanations necessary for a better understanding of the other synthetic documents and completes the information in certain limits or presents the information in another form*”. (Ionescu, 2003)

Most of the information that must be presented in the annex is stipulated in the Directive’s article 43, completed however by other articles, pointing out that certain information from the balance sheet and the profit and loss account must be detailed in the annex if they are of significance.

So, it must be presented in the annex information regarding:

- The evaluation methods applied to the different positions in the financial statements as well as the calculus methods for value corrections (amortizations and provisions);
- Information concerning the interests held, for at least 20% from the capital of the issuer companies;
- The number and nominal values of the various categories of shares that compose the capital;
- The number and size of the beneficiaries’ rights, of the transferable bonds and other similar securities;
- The debts’ dimensions, especially for the ones older than five years;
- The size of the financial engagements besides the balance sheet;
- The turnover’s structure on categories of activities and geographical markets;
- The average number and structure of the employees, during the budgetary year;
- The incidence of the derogative fiscal evaluations on the net result of the budgetary year;
- The dimension of the postponed taxes;
- The size of the remunerations for the administrative, management and control personnel;
- The dimensions of the advances and credits given to the administrative, management and control organs as well as the engagements taken on their account, based on some guarantee.

In the article 44, the 4th Directive mentions the national accounting systems of the member states of E.U. can establish an abbreviated annex for the small and middle enterprises.

In the opinion of the Romanian standardization organism, the **annex** is substituted by the **Explanatory Notes** to the financial statements containing supplementary information, relevant for the users' necessity regarding the financial position and the results obtained.

The national accounting norms impose a pre-established structure of this set of situations forming the **Explanatory Notes**, but also a presentation model for certain notes, considered adaptable to a certain format of annual financial statements.

It must be noticed that these documents are equally important and brings about the same amount of responsibility for those elaborating and signing them in the Romanian financial reporting system.

The 10 Explanatory Notes present in a systematic manner each significant element of the balance sheet, of the profit and loss account, of the treasury and of the shareholders' equity.

The information that must be presented by the annex (explanatory notes) in the national financial reporting system are referring to:

1. Presentation of the accounting policies adopted by the enterprise for the evaluation of elements from the balance sheet, the results account, the cash flows and the shareholders' equity variations;
2. Details regarding intangible assets and provisions for liabilities and charges;
3. The manner in which the profit gained is allocated;
4. Information concerning the analysis of the operating incomes;
5. Information about the debentures and debts' situation;
6. Number and value of the shares and securities that compose the capital;
7. Information concerning the employees and the members of the administrative, management and supervision structures' remunerations;
8. Information regarding the alternative accounting policies applied in the enterprise;
9. Examples of calculus and analysis of the principal economic-financial indicators;
10. Other information concerning the presentation of the enterprise, its relations with other branches or enterprises, the size of postponed taxes and of the turnover on economic sector and markets, the remunerations paid to the auditors, the engagements given and received etc.

We point out the fact the contents of the annex as stipulated in art. 43 of the directive are also to be found in the contents of the Explanatory Notes from the national financial reporting system. But the informational value of the Explanatory

notes is higher than that of the Annex, because they have a larger opening towards the financial analysis, underlining in the Note 9 „*Examples of calculus and analysis of the principal economic-financial indicators*” characteristic for the activity of an enterprise.

Generally speaking, **the information given by the annex completes and comments upon the information offered by the other annual financial statements.**

These documents with accounting and extra-accounting character offer only information of significant importance to the users, being an excellent mean of informing and analysis.

The Annex's analysis allows the users to achieve a better understanding, especially of the balance sheet and of the profit and loss account, offering relevant supplementary information regarding the enterprise's financial position and the results obtained by it.

The role of this situation is to be found greatly in the amelioration process of the synthetic and annual reporting accounting documents' informational value.

The elaboration of the annex is made based on the **principle of good informing**, according to which the annex must include any information necessary to the users.

At the same time, even the conceptual motivation of the annex represents the consequence of some accounting principles' putting in practice, most of all **the principle of significant importance and the principle of the true and fair image.**

Therefore, besides the compulsory information stipulated by the Directive, it will be mentioned any information considered necessary and significant for obtaining the true and fair view.

*Consequently*, the annex to the annual financial statements must offer information regarding the synthetic accounting documents' elaboration principles and the specific accounting policies, selected and applied within those, information that are required by the 4th Directive and are not stipulated in other statements, as well as additional information necessary for the achievement of the objective to reflect the true and fair image, the financial situation and the results obtained.

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