Royal Decree 1/2021, of January 12, which amends the Spanish National Chart of Accounts (CoA) and additional legislation, in accordance with international accounting standards.

In line with the draft amendment to the Spanish National Chart of Accounts (CoA) and additional legislation published by the Spanish Accounting and Auditing Institute – Instituto de Contabilidad y Auditoría de Cuentas (ICAC) - in October 2018, the amendment to the Chart of Accounts and its additional legislation is finally approved by Royal Decree 1/2021 of January 12.

The main objective is to adapt internal accounting standards to the standards approved by both EU-IFRS 9 Financial Instruments and EU-IFRS 15 Revenue from contracts with customers, the affected CoA regulations being the 9th (financial instruments), 10th (inventories) and 14th (revenue from sales and services rendered).

The application of this Royal Decree affects fiscal years beginning on or after January 1, 2021, and the main amendments are as follows:

1. New regulation on revenue recognition.

The approval of the Royal Decree means having an independent and autonomous internal accounting regulation for the relevant tax and mercantile implications it produces, but at the same time, it is fully adapted to EU-IFRS 15. However, many of the clarifications introduced by EU-IFRS 15 have already been dealt with by the ICAC through resolutions and consultations.

The amendment is based on incorporating into the CoA the basic principle of recognising revenue when control of the goods or services committed to the customer is transferred and for the amount expected to be received from the customer, based on a five-step sequential process.

Therefore, from now on, when we recognise income, we must follow the following analysis, which consists of five successive stages:

1. Identify the contract(s) with the client, understood as an agreement between two or more parties that creates enforceable rights and obligations.

2. Identify the obligations to be fulfilled to transfer goods or provide services: in this sense, it is necessary to establish whether the obligations are individual, which leads to the recognition of the revenue of that good or service or, on the contrary, whether they are combined with others.

3. Determine the transaction price.

4. Assign the price of the transaction among the obligations to be fulfilled: this should be done based on the individual selling prices of each different good or service committed to in the contract or following an estimate of the selling price when the selling price is not independently observable.

5. Recognise the revenue when the company fulfills an obligation:
   - Over time: in which case revenue will be recognised based on the degree of advance, or
   - At a point in time: income is recognised on that date.

In relation to the information to be included in the report that had been previously required, there is a significant change since it has now been decided to incorporate all the information requirements of the CoA.

These changes in the recognition and valuation of revenue from the delivery of goods and services must be applied retroactively, in accordance with recording and valuation standard 22nd of the CoA, using one of the following two options:

A) If the company decides to restate the comparative information, it should take into account whether the contracts have been discharged, whether they have variable consideration or whether they are modified before the beginning of the previous year and, in any case, apply the principle of uniformity to all contracts.

B) If the company decides not to restate comparative information, it may choose to apply the new criteria retroactively only to contracts not discharged at the date of first application.

⇨ As an alternative practical solution: the company may choose to follow the criteria in force until December 31, 2020, for contracts that were not discharged on the date of first application (i.e. January 1, 2021, for a company whose fiscal year coincides with the calendar year).

2. New regulation on financial instruments.

With respect to financial instruments, the following modification should be noted in relation to classification and valuation.

The main change is in the “Available-for-sale financial assets" portfolio, which is renamed "Financial assets at fair value with changes in the equity.”

Therefore, for valuation purposes, financial assets are included in one of the following categories:

1. Financial assets at amortised cost.

2. Financial assets at fair value with changes in the profit and loss account.

3. Financial assets at cost.

4. Financial assets at fair value with changes in the equity.

Thus, the comparative classification of financial assets before and after the reform would be as follows:

FINANCIAL ASSETS BEFORE 2021	**FINANCIAL ASSETS AFTER 2021**
Loans and receivables	Financial assets at amortised cost
Held-to-maturity investments	
Financial assets held for trading	Financial assets at fair value with changes in the profit and loss account.
Other financial assets at fair value with changes in the profit and loss account	
Investments in the equity of group, multigroup and associated companies.	Financial assets at cost.
Available-for-sale financial assets	Financial assets at fair value with changes in the equity.

In addition to these classification criteria, two accounting method options have been introduced:

- Valuate at fair value with changes in the profit and loss account any financial asset, except for investments in group, multigroup, and associated companies, provided that this simplifies the accounting process and avoids accounting inconsistencies and asymmetries.

- Valuate an equity instrument in the fair value portfolio with changes in the equity on the initial recognition date.

In relation to financial liabilities, for valuation purposes, they will be included in one of the following categories:

- Financial liabilities at amortized cost.

- Financial liabilities at fair value with changes in the profit and loss account.

Notwithstanding the foregoing, contributions received as a result of accounts agreement and similar agreements are valued at cost, increased or decreased by the profit or loss, respectively, to be attributed to the non-managing participants.

The same criterion will be applied to participating loans whose interest is contingent. Finance costs are recognised in the profit and loss account on an accrual basis, and transaction costs are charged to the profit and loss account on a straight-line basis over the life of the participating loan.

Also, as part of the measures approved to simplify the accounting method for financial instruments and with respect to hybrid financial instruments, the requirement to verify and separate the implicit derivatives in a main contract that is a financial asset has been eliminated.

Therefore, they are valuated at amortized cost if their characteristics are those of an ordinary or common loan, or otherwise at fair value.

Another of the issues already raised in the Draft Royal Decree is related to hedge accounting, in which the aim has been to align the accounting result and risk management, introducing greater flexibility in the requirements to be met for the provisioning of these hedges.

In this sense, companies are temporarily allowed to continue applying the criteria that have been applied up to now.

3. New inventory regulation.

In line with EU-IAS 2 Inventories, the fair value less costs to sell criterion is introduced in the regulation for recording and valuating inventories, as an exception to the general valuation rule, for intermediaries that trade listed commodities. That is, when they are part of trading operations.

4. Other changes.

With the approval of the modification of the CoA and in accordance with EU-IFRS 9, the change in the "Available-for-sale financial assets" portfolio makes it necessary to revise part of the regulations for the preparation of annual accounts, balance sheet models, statement of recognised income and expenses, as well as the profit and loss account.

With regard to the Rules for the Preparation of Consolidated Financial Statements, in line with the modifications to the individual accounts; this is as a result of the change of portfolio denomination mentioned above and also with the objective of introducing the same information requirements in relation to the accounting processing of financial instruments and the recognition of income from the sale of goods and the rendering of services.

Regarding the Spanish National Chart of Accounts for Small and Mid-Sized Companies, the amendment is made to introduce a technical improvement related to the regulation on fair value, the criterion for accounting for the application of the result in the partner, with the appropriate criterion for the presentation of capital issues and the regulation for the preparation of reports. However, with respect to financial instruments, the recognition and valuation criteria have not been modified in order to simplify the accounting obligations of smaller companies.

Regarding non-profit entities, it is modified in order to align the annual accounts models to the changes introduced in the recording and valuation regulations of the CoA.

Note: This document is of an informative nature and in no case dose it imply individualized accounting advice.