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STATEMENT OF CASH FLOWS - DYNAMIC IMAGE OF CHANGES IN FINANCIAL POSITION OF AN ECONOMIC ENTITY

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Annual financial statement users want the best possible information about the ability of economic agents to make payments, liquidity needs, as well as for comparing different company's results, eliminating the impact of using different accounting methods for similar transactions. For this purpose it is necessary cash flow statement.According to a survey[14] of 78 companies listed on the London Stock Exchange, the cash flow statement is especially useful in "Treasury analysis from operating activities" and "coverage determination of dividends and interest cash flows net of tax ".

JEL Classification: G30, C32

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1. Introduction

In Romania, according to. Article 3. (1) Order no. 3055 of 29 October 2009 approving the Accounting Regulations in accordance with European directives, the cash flow statement is considered part of the annual financial statements, together with: balance sheet, income statement, statement of changes in equity, notes to financial statements[15].At international[16] level preparation for this is required by IAS 7 Cash flow statement, in which it is stated that the **treasury** (cash) means money in the counter and money in bank demand deposits.

Flows equivalents (cash equivalents) are short-term investments, highly liquid, which can be easily converted to cash, to known amounts and the risk of changes in value is negligible.These cash equivalents are held rather to cope with short-term cash commitments rather than for other purposes. An investment will not be considered generally equivalent flows unless an approaching maturity, for example less than or equal to three months from the date of purchase.Generally, shares are excluded from cash equivalents.

In turn, the cash flows are inflows and outflows data items as cash or cash equivalents. Cash flows exclude movements between items that constitute cash or cash equivalents.

In this context, even if, for example, loans taken from banks are generally considered to be financing activities in some countries, current overdraft repayable on demand form an integral part of cash management firm, where part category of cash and cash equivalents, if not in the cash flow statement.

Meanwhile, the treasury has a vital importance for the enterprise, through the size and by it sign (positive or negative) because to characterize the situation in which it is situated (financial health, vulnerability, bankruptcy, etc.) and therefore shows reflection on company's financial position with equity.

[14]FRS 1 Cash flow Statements-a new technique for financial analyses, de J.M. Broadbent, B.W. Webb şi T. Hassal, quote de M. Ristea (1996)
[15]OMPF 3055/2009, art. 3, (1)
[16]In Romania, the first regulation issued on harmonization with Directive IV of the EEC and International Accounting Standards (OMF no. 403/1999) cash flow statement include among annual financial statements, but does not provide information on the content and how to prepare it. Subsequently, by Order no. 94/2001 and now by Order no. 3055/2009, it has remedied this shortcoming. Receipts and payments are presented in detail to the example given in the Annex to IAS 7 Statement of Cash Flows, but no fund differences to international regulation.

2. The provisions of IAS 7 on cash flow

Information about the cash flows of a company is useful because they allow users assessing the ability of the enterprise to generate flows items and cash equivalents and its cash needs.

IAS 7 is applicable to all companies that are required to draw a statement of cash flows, regardless of their activity. This is justified by the fact that, in essence, enterprises, regardless of the type of business or organization they need cash for the same reasons: the need to be able to exercise their activity, pay the debts and provide a return to investors.

The cash flow statement allows, if it is used together with other components of the annual financial statements, the assessment of changes of the company net asset, its financial structure (including its liquidity and solvency) and its ability to change flows (size, meaning and their maturities) to adapt to new circumstances and new opportunities.At the same time, users can develop models that enable them to judge and compare future cash flows of many companies.

Still here it may be mentioned that the presentation of cash flow improves comparability of different businesses operating performance because it eliminates the effects of rules and accounting treatments for like transactions and events which may differ from one company to other.With the use of this situation to estimate future cash flows, it can retain and to verify the accuracy of the estimates made previously.

The cash flow statement should answer to these requirements and flows that are classified according to the nature of the activities of the enterprise:

- cash flows from operating activities;[17]
- cash flows from investing activities;[18]
- cash flows from financing activities;[19]

A. Operating activities

The size of the cash flows arising from operating activities is a key indicator of the extent to which the operations of the enterprise have generated sufficient cash to repay loans to maintain the operational capability of the enterprise to pay dividends or to make new investments without recourse to external resources.

In essence, operating cash flows results from the main income generating activities of the enterprise from transactions and other events that are taken into account in determining the net result, for example:

- cash inflows from the sale of goods and services;
- inflows of money from royalties, fees, commissions and other revenue;
- cash outflows to suppliers for goods and services;
- outflow of money to employees or their equivalent;
- cash inflows and outflows of an insurance company on assurance premiums and compensation, and other benefits related to insurance premiums;
- tax payments, except the part which may be associated directly to investing or financing activities;
- inflows and outflows of cash arising from contracts held for negotiation or trading;

Particular transactions, such as the sale of an item of fixed assets, may give rise to gains or losses are taken into account in determining the net result. Flows generated by these transactions are but investment flows.

A company may own titles and assets for trading purposes, they are so similar to inventory purchased to be sold (goods) and, consequently, the corresponding cash flows from operating activities are classified.

Similarly, cash advance payments and loans made by financial institutions are generally considered operating flows, as they are the main business of this type of enterprise.

B. Investment activities

The separate disclosure of cash flow related to investment activities is important because they indicate the extent to which efforts were made to increase resources intended to generate future income and cash flows. The main such flows are:

- outflows of money in order to purchase the tangible fixed assets, intangible assets and other long-term assets[20];

[17]Through operating activities is meant the main income generating activities for the company and any other activity that is not investing or financing.
[18]Investing activities are the entry and exit of long-term assets and assets in the form of investments that are not cash equivalents.
[19]Financing activity is an activity which results from changes in the size and composition of the equity and loan companies.
[20]This includes also development costs as well as expenses incurred for obtaining of property from own production.

- cash inflows from the sale of long-term assets;
- cash outflows for the purchase of shares, shares, bonds and other similar instruments other than those intended to be held for trading;
- cash inflows from the sale of instruments of the kind mentioned in the previous paragraph;
- loans granted (other than those granted by financial institutions);
- inflows of money from repayment by borrowers of loans (except those granted by financial institutions);
- cash outflows on account of contracts on terms, options and swap contracts unless such contracts are held for trading or are considered financing activities;
- cash inflows from contracts on terms entered into on organized markets from options or swap contracts, unless they are held for trading or fall from financing activities;
- When accounting for a contract to cover the risk of an identifiable position, the cash flows are classified as flows generated by the hedged position.

C. Financing activities

Separate disclosure funding streams is useful for making predictions about the expected flows to equity investors who gave to the company:

- cash inflows from issuing shares or other equity instruments;
- outflow of money from the redemption of its own shares;
- Proceeds from usual borrowings to the debt securities of treasury bills, mortgage loans and other long-term loans or short term;
- cash outflows for repayment of contracted loans;
- Payments made by the person who takes a financial leasing contract, to settle long-term debt balance related.

The separate disclosure of these flows allows assessment of the effects of each of the activities on the financial situation of the company as well as relationships that may arise between activities.A single transaction may be composed of different stream classes. Thus, rate on the loan amount paid may include both interest - which can keep operating activities and capital return is certainly a financing operation.

3. Methods of presenting cash flows

Considering that European directives do not provide a model of the cash flow statement, as applicable balance sheet and profit and loss account, "the source of inspiration" for Order no. 3055/2009 for this component of the annual financial statements was represented by IAS 7. Thus, as the international standard, a firm may present cash flows from operating activities by applying one of the following methods:

- **direct method**, whereby major inputs and outputs are presented gross cash;
- **indirect method**, whereby flows reconstruct operation based on net income is adjusted to *be eliminated*: no effect on treasury transactions, gaps or regularization of past or future inputs and outputs on the treasury, items of income and expenses related to cash flows from investing and financing activities.

Businesses are encouraged to use the direct method because it provides information that is not available when using the indirect method.

According to the direct method, information about the main classes of gross cash inflows and outflows can be obtained as follows:

- on the basis of records performed by the undertaking;
- by adjusting sales, cost of sales and other elements of the income statement to take account of:
- variations during the period of inventories, receivables and operating liabilities;
- other items with no effect on the treasury;
- other items for which the effect on investment flows consist of treasury or finance.

According to indirect method, cash flows from operating activities are determined by adjusting net income to take account of:

- variations during the period inventory, receivables and operating liabilities;
- elements without effect on treasury such as depreciation, provisions, deferred taxes, gains or losses latent undistributed benefits associated enterprises, minority interests;
- other effects on the treasury elements consist of financing or investment .

Cash flows from operating activities may be presented under the indirect method and the indication of revenue and expenses in the income statement during the year with variations stocks, receivables and operating liabilities.Some cash flows from operating activities or financial investment which can be presented as a net amount. These are:

- inflows and outflows of money on behalf of clients when flows arising from the activities of the customer and not of the enterprise[21];
- inflows and outflows of money on items that have a high rotational speed they have a large and short term[22]

In the case of financial institutions it can be presented their net size following feeds:

- inflows and outflows of cash on the acceptance and repayment of deposits with maturities determined;
- deposits made other financial institutions also to withdraw those deposits;
- loans made to customers also the repayment of these loans.

In the cash flow statement, the company must submit the main categories of inflows and outflows of money, except flows can be presented as a net amount.

The direct method uses information like receipts and payments; treasury variation on mining operations is equal to the sum of receipts and payments.Information regarding the major classes of receipts and payments are not offered directly on the financial statements. These can be obtained directly from the accounting records or indirectly through adjustments. The amount of sales made during the year usually does not coincide with the proceeds from the sale period. In order to determine information on customer receipts data are needed from both the balance sheet and profit and loss account.

This method is recommended for the businesses, being understood by users, allowing presentation overall cash movements also being able to obtain information on the sources also use of any cash. It is also preferred by the investors, providing information useful in forecasting future cash flows.

The indirect method is approved by the company management because hides real internal users on the liquidity and solvency of the company. It basically uses the information provided by accrual accounting and *highlights the differences between operating profit and net cash flow derived from operations.*The method involves actually drawing of a picture to reconcile net income before tax and extraordinary items net cash flow from operating activities.

In practice, most companies are opting for the indirect method because a modern accounting system calls accrual. It is also approved by the company's accountants, and can be easily obtained by taking the existing data on the balance sheet and profit and loss.

The cash flow statement is an important tool in the management of any business because it *provides information regarding the presence of cash accounting surplus / deficit effective to supplement the information on the profit or loss resulting from the application of accrual accounting.*

The business is basically an integrated system of cash-flows driven by management decisions. Analysis of cash flow statement is the basis for investment decisions and financing business operation. It is also an economic and financial analysis tool that those responsible for decisions are helped to make good decisions using relevant information to determine:

- capacity expansion of an entity based on the entity's internal financial results;
- entity's ability to generate cash from its activities;
- information on the ability of firms to generate cash and solvency in the medium and long term.

On the calculation method of cash flows, IAS 7 recommended direct method, thereby providing useful information for estimating future cash flows and using the indirect method the information is not available. In practice, enterprises prefer the indirect method of calculation as it has a logical size closer to accounting reports.

4. The usefulness of cash flow statement (cash flow)

A statement of cash flows as part of the financial statements reveal their usefulness in following directions, as they are listed in the accounting rules:

a) Ensuring quality of accounting information

Through its content, the cash flow statement is circumscribed to the general direction of standards to ensure the quality of information, including comparability. Comparisons in space, between businesses, are facilitated by the following:

- operating results (in our opinion, even in this case we consider the current results) reported by different entity of the same sector are comparable due to the specific procedures for income and expense recognized in accounting terms.This is removal of the cash flow statement of those revenues

[21]It may frame here: acceptance and repayment of deposits held by a bank, treasury held on behalf of a client by a firm specializing in investments, rents paid to the owners of goods after they have been collected for them.
[22]Are included in this category: loans to credit cards, purchase or sale of investments and other short-term loans, such as those with a maturity of less than three months.

and operating expenses (but financial and others) considered "calculated". They do not generate receipts and payments in the course analyzed and determined cash flows. Such items are depreciation expenses, provisioning expenses and income, income from investment subsidies etc.The consequence is that the current result is not influenced differently as a company has opted for straight-line depreciation, digressive or accelerated for the same type of fixed assets. Also, the tax considerations that influence a company when it decides to establish provisions, doesn't affect the current result, considering that they are not taken into account.Finally, the current results accurately reflect the intrinsic performance of the company, now which is not influenced by the subsidies can only be received by certain enterprises, even belonging to the same sector.

- as it will develop below in section c) cash flows for the periods listed are the basis for estimating future cash flows, and hence, the value of the company. As published in the financial statements is a valuable material for an external analyst may thus achieve assessments (through methods yield) and comparisons between companies whose heterogeneous data are unified through the concepts of value and market connection.

b) Possibility of carrying out financial analysis

Accounting information is useful when it helps to take grounded correct economic decisions. In the decision-making process are concerned management techniques using specific tools of financial analysis and economic evaluation of the business.It is understandable then additional informational contribution of financial statements that provide mainly through cash flow statement, a database of partially processed financially and economically.

c) Opportunity to assess business (businesses)

Business evaluations as a branch of economic evaluations, market, are highly appreciated by the users of accounting information, because it allows estimating alternative business strategies and programs of the strategies (initiation of new products, entering new markets), the evaluation major transactions - mergers, acquisitions, sales, recapitalizations, share issue, communication with partners, especially with shareholders about the business value (plans, strategies), value-based management application for forwarding performance of various activities of the company (when, how and how to expand businesses that bring value to the operational measures has the best chance to increase the value).

Between business valuation methods the most used are methods of yield. In the values obtained - values yield - the most widespread and the highest coefficient of importance they have the values obtained by discounting cash flows (cash flows or cash). This derives from the benefits that they offer cash or results received to accounting results. Thus:

- cash is an objective concept, easily understood and perceived;
- users of financial statements (shareholders, creditors, others) have a priority interest on the monetary aspect of transactions of such entity to the detriment of accounting earnings or other indicators of activity;
- cash or cash flow forecasts for past periods serve the financial policy of the company's short and long term. For a given company, the cash flows are differentiated by three cycles of its specific activity as shown above.

Conclusions

I hope I have demonstrated thus great utility that has cash flow statement which complies with the above classification for business valuation. Of course, the flows are historical; rebound all can be sold as such or by estimation based on their future cash flows.

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