

What means in fact the cash accounting?

Cristina Baban

Abstract:

Even if it is talking more and more in the accounting craft about as it is named "cash accounting" we don't know yet what it represents, except a definition which recommends that it takes into consideration only the operations that use liquidities.

We are now witnesses of some new improvements of the international accounting standards and especially those which are referring to the Cash Flow Statement (IAS 7). So, we must analyze them and we must purpose some others that could make much easier the interpretation of cash and treasury information of a company in a crisis period.

Keywords: cash accounting, international accounting standard, treasury, liquidities, crisis period, cash budget, cash result.

INTRODUCTION

We are proposing to present which are the reasons for according more attention to cash accounting by implementing it not just discuss it.

Also, we will take into consideration the new improvements of IAS 7 (from April 2009), and we going to purpose that all operations which use cash must be recorded on special accounts and not just basing on the other statements for the Cash Flow Statement.

Regarding this aspect we will expose shortly the cash budget process and the cash result that a company must present

DEBATING THEME

For many firms to present a Cash flow statement is not an obligation, exception is given by some big companies that are using the international accounting standards. Even though, these companies are resuming their cash statements to a sample list of cash inflow and cash outflow for each activity: operating, investing and financial.

Starting from the premise that Balance Sheet states and tries to measure the amount of wealth owned by stockholders and Profit and Loss Account is measuring the net profit earned by the firm in a given period we are able to say that both are based on the accrual accounting. So, the engagement accounting express only the present incomes and expenses which are engaged for the moment and not only the cash in-outflow, which are paid or collected by the company.

For this reason the cash aspect is not well reflected in these statements. That's why is not necessary only to present the cash flow statement but also to improve it as possible it is, and not being just a simple facultative statement for small and medium companies, and for the big ones to be more expressive and not a list of cash in/outflows.

Regarding this aspect we must start from the cash budget that is related to the inflows and outflows of money. It represents a mirror of company's liquidities for each period, being a projected financial statement of cash evolution.

It is recording all expected inflow and outflows, registering the moment of their occurrence. So, it is recommended to look at the past operations for assuming that it will repeat for the next period. This aspect is the most important tool to evaluate the company's liquidities.

In practice, this moment of elaborating the cash budget is quite frequent eliminated from the economic department of some firms and companies. So, the examination of cash budget will allow the decision maker to choose an alternative in financing activities or investment of the surplus cash from the operating activities.

Regarding this aspect we will present four steps that could help in the elaborating cash flow budget:

1. the liquidity expenses must be reduced as possible it is (we buy only what is necessary for the company and not the last car, PC or telephone)
2. it must be truly realistic by estimating daily or weekly the collects and payments
3. it must take into consideration that not all clients will pay at time, so we mustn't let them to be late
4. it must be update with all expenses that change into payments and all revenues that change into collects

So, the final statement – Cash Flow Statement must be a result of cash budget process that is realized from the beginning period (monthly, quarterly, or for a year).

In the last time we are talking about as it is named “cash accounting”, but we must to analyze it in parallel with the engagement one. Each of tow has their pluses and minuses.

Now, in practice is used more the accrual accounting, but it is also recommended to record all operations in their evidences basing on the cash accounting even it isn't reported it must be practiced any time, for avoiding as possible it is a cash crisis period.

We are using the term of cash accounting but in fact it is not basing on account recordings. Also, the cash flow statement doesn't base on the registering all operation basing on the accounts (like other tow statements – Balance Sheet or Profit and Loss Account).

Looking to this issue we are proposing to record all operations which use liquidity on special accounts. Even if it is too hard, in practice, we are recommend to use two groups of accounts from the 5th classes, one for inflows operations (that function like an assets account) and other for outflows operations (like a passive one), that may be divided into analytics for every activity. All that will close through a general cash account.

So, for a good evaluation of cash situation we must base on recording the cash in / out flow, and not base on the Balance Sheet and Profit and Loss Account information. This kind of purpose is recommended especially for the crisis period when we must know which is the influence of each activity and operation on the final value of cash.

Finally, Cash Flow Statement will be just like Profit and Loss Account but referring to the cash situation.

Regarding the new update of the international accounting standard IAS 7 from April 2009 this is an adding on the investing activity aspect. So, “only expenditures that result in a recognized asset in the statement of financial position are eligible for a classification as investing activities”.

It is an important clarification and the amendment explains which are the conditions to classify an expenditure resulted in an asset as cash flow from investments, because the misinterpretation of standard or a part of it could generate some irremediable mistakes.

So the result from the treasury accounting is more important then profit based on accrual accounting that may be tricky, because it is basing on future cash flow that will be obtain and not on the estimate profit.

Consequently the cash result will looks like:

- profit and loss account before tax
 - + / - adjustment from the non monetary elements
 - + / - change of current assets and debts
 - + / - cash flow from investment activities
 - + / - cash flow from finance activities
 - tax profit paid
 - = cash result

Finally we may say that we start from the profit to achieve the cash result by adding or cutting all elements that influenced the treasury situation.

CONCLUSIONS

This article presents shortly some treasury aspects on that depends the healthy of a company.

I was trying to present the cash budget importance and that is the start of liquidity evolution in a determinate period that ends with the Cash Flow Statement.

Also I was trying to suggest that a cash accounting must use accounts recordings and Cash Flow Statement must base on them and not on information from other statements. So, the standard IAS 7 is open to be update once the economical, financial, international and national aspects it requires for it.

REFERENCES

- [1] Ignacio Velez-Pareja – Construction of free cash flows – a pedagogical note, 2001
- [2] <http://papers.ssrn.com/paper> - available on line
- [3] Amendment to IAS 7 – Statement of Cash Flow and Addition of Basis for Conclusions on IAS 7 Statement of Cash Flows – April 2009
- [4] IASB Update – Annual improvements – June 2008 - www.iasb.org – available on line
- [5] Prof. PhD. Mihai Ristea, Graziela Dumitru, Ass. Alina Mihaela Curpan – Libertate si conformitate in contabilitate (Freedom and compliance in accounting) – Ed. CECCAR, 2008

Contacts:

Baban Cristina Lucia, PhD Student Academy of Economic Studies Bucharest Romania, E-mail: cristina_baban@yahoo.com

The report is reviewed.