

Treasury Flows Overview

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Introduction

The overview of the treasury flows presents such flows, known as incomings and pays, during the specific period. In other words, it shows where the liquidities have come and how they were spent, explaining in this way the causes of their variation.

The treasury flows overview has the following purposes:

1. It allows the prevision of future treasury flows.
2. It allows the evaluation of the decisions taken by the management.
3. It allows the determination of the capability of the company to pay dividends to the shareholders, to pay back the loans granted by the creditors and to pay the interests to the creditors.
4. It shows the relation between the net result and the treasury flows of the company.

The objective of the norm IAS 7 “*Cash flow statements*” is to draw the making, presentation and publishing politics corresponding to this financial situation.

No matter which is the main activity that generates incomes, the companies need treasury elements in order to conduct its activities, to pay their obligations and to ensure reliability for their investors.

The **liquidities** (cash) refer to the available funds and to the call deposits.

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The **treasury flows** (cash-flows) mean the assembly of liquidity entrances and exits and liquidity equivalents.

The **treasury flows** do not include the movements between the elements that seen as liquidities or liquidity equivalents, because they are not part of the treasury management of the company.

The **managements of the treasury** include the placement of the surplus reserve and liquidity equivalents.

The **liquidity equivalents** are short-term placements, highly liquid, that can easily be converted in a measurable amount of liquidity and that are exposed to a risk to change in value that can be neglected.

The **titles** that represent shares are excluded from the liquidity equivalents. Are excluded the privileged shares bought just before their overdue and that have a well determined redemption date.

If the **banking loans** are mainly elements for the financing activities, call redemption short term loans, granted by the current accounts are included in some countries in the category of liquidities or liquidity equivalents.

The **treasury flow overview** must present the treasury flow of the exercise classified in exploitation, investments and financing activities.

Some transactions can include treasury flows that are classified in many activities. For example, in the case of the redemption of a loan using treasury exports, the payment refers to interests, as well as to the borrowed capital. The part corresponding to the interests can be classified as exploitation activities, while the part corresponding to the borrowed capital is classified as financing activities.

The treasury flows generated by the exploitation activities

The treasury flows generated by the exploitation activities are essentially the consequence of the main activities that generate income for the company, and subsequently they result from transactions and other elements that concur to the formation of the net result.

From this category the following take part:

- Incomings that derive from the sale of goods and service providing;
- Incomings that come from royalty, fees, commissions and other incomes;
- Payments regarding the debts towards the goods and services suppliers;
- Payments for the employees and payments in the account of the employees;
- The relative incomings and payments for premiums and calamities, annuities and other benefits connected to the insurance policies, in the case of an insurance company;
- Payments and paybacks of taxes upon profit, with the condition that these cannot be specifically associated to the financing and investments activities.

Some transactions, like the cession of an immobilisation like the production installations, can generate a plus or a minus of value, which affects the net result. Although, the treasury flows related to this kind of transactions do not belong to the exploitation, because these operations are under the incidence of the investments activities.

A company can have titles for commercial use, in which case these are similar to the stocks bought in order to be sold at a later time. As a result, the treasury flows that come from the acquisition of titles take for commercial purposes are included in the category of exploitation activities.

Treasury flows generated by investments activities

The IAS 7 Norm shows that the flows that result from investments activities indicate the measure in which the payments have been done for the acquisition of actives destined to generate incomes and future treasury flows.

The treasury flows generated by the investments activities offer information about the manner in which the company ensures its long duration and growth. They refer to:

- Payments made for the acquisition of corporal and non-corporal immobilisations, as well as other long term actives, including the capitalised developing expenses and the payments implied by the immobilisations produced by the company for itself;
- Incomings that come from the selling of corporal and non-corporal immobilisations, as well as the selling of other long term actives;
- Payments made for the acquisition of participation titles and emitted claim titles or claims from other companies, as well as the payments made for the acquisition of participations to the joint-venture companies (others than the payments made for the instruments considered as being equivalent liquidities or held for commercial purposes);
- Relative incomings at the sale of participation titles and claim titles emitted or claims from other companies, as well as relative incomings from the sale of participations to joint-venture companies (others that the incomings generated by instruments considered as being equivalent liquidities or held for commercial purposes);
- Treasury down-payments and loans granted to third parties (other than the down-payments and loans granted by a financial institution, that belong to the flows generated by the exploitation activities, for such entities);
- Incomings that derive from the redemption of treasury down-payments and the loans granted to third parties (other than the down-payments and loans granted by a financial institution); etc.

Treasury flows generated by financing activities

The financing activities are those activities that generate changes in the size and the structure of owned capitals and loaned capitals of the company.

The separate presentation of these flows within the treasury overview is given by the possibility to use these in the prevision of the sums that the shareholders and the capital creditors will withdraw from future funds (capitals). The treasury movements generated by the financing activities refer to:

- Incomings from the emission of shares and other own capital instruments;

- Payments made towards the shareholders for the purchase or repurchase of the shares of the company;
- Incomings from the emission of obligation loans, banking loans, treasury tickets, mortgage loans and other short term or long term loans;
- The redemption with cash of the borrowed sums;
- Payments made by the renter for the reduction of the debt balance referring to a financing-location contract.

Methods to present the treasury flows referring to the exploitation activities

A company must present its treasury flows, afferent to the exploitation activities, using:

- **The direct method**, according to which the supplied information refers to incomings and payments in their gross values;
- **The indirect method**, according to which the result is adjusted in order to take into account:
 - The influence of the operations that do not have a monetary character;
 - The elements of the incomes and expenses associated to the treasury flows that regard the investments or the financing activities;
 - The influence of the necessary elements variation within the working capital upon the treasury.

In order to understand the variation of the necessary elements within the working capital, we start from the following calculus relation:

$$\boxed{\begin{array}{c} \text{Necessary working} \\ \text{capital} \end{array}} = \boxed{\begin{array}{c} \text{Exploitation} \\ \text{actives} \end{array}} - \boxed{\begin{array}{c} \text{Exploitation} \\ \text{passives} \end{array}}$$

Exploitation actives consist of stocks, debts towards the clients and assimilated accounts, other exploitation debts and, by assimilation, expenses in advance.

Exploitation passives consist of debts towards the suppliers and assimilated accounts, other exploitation debts and by assimilation, at least partially, the incomes in advance.

The IAS 7 Norm encourages companies to present information regarding the treasury flows generated by the exploitation activities using the direct method. This method uses treasury flow information types (incomings and payments), information that can be useful in order to estimate future treasury flows.

The direct method to present the treasury flows afferent to the exploitation activities:

+	Incomings generated by the relationships with the clients
+	Incomings that come from royalty, fees and other incomes
-	Payments towards the suppliers
-	Payments in favour and for the personnel
-	Interests and paid dividends
-	VTA payments
+	Other incomings generated by the exploitation
-	Other payments generated by the exploitation
-	Payments regarding the tax upon the benefits
±	Extraordinary elements
=	<hr/> The net treasury flow from exploitation activities

The indirect method consists of making a reconciliation table for the net result before the applying of the tax that also has extraordinary elements with the net treasury flow from exploitation activities. A typical presentation, in agreement with the IAS 7 Norm, of the procedure developed using the indirect method, is presented in the table below.

±	The result before the applying of the tax and the extraordinary elements	
	The elimination of the incomes and expenses without effect upon the treasury	
+	The expenses regarding the redemption and the provisions	
–	Incomes from redemptions and provisions	
	The elimination of the incomes and expenses not connected to the exploitation	
±	The result of the cession of the immobilisations	
±	The result of cession of placement titles	
+	The expenses regarding the interests	
–	The incomes from interests and dividends	
–	Subventions for investments paid towards incomes	
=	± The result from the exploitation before the variation of the necessity within the working capital	
±	The variation of stocks	
±	The variation accounts-clients and of other exploitation receivables	
±	The variation of expenses in advance	
±	The variation of the accounts of the suppliers and the variation of other debts from exploitation	
±	The variation of incomes in advance (from exploitation)	
	Other works that require incomings and payments type information	
–	Interests and paid dividends	
–	Payments regarding the taxes upon the benefits	
±	Extraordinary elements	
=	The net treasury flow relative to the exploitation activities	

Preliminary explanations to understand the indirect method:

- The eliminated expenses are taken with the plus sign, and the eliminated incomes, with the minus sign, because in the calculus of the result (in the context of the profit and losses balance) they have been taken with the minus sign and respectively with the plus sign.
- The result of the assignment is a net income or a net expense and it follows the elimination line presented at point number 1.
- In the case of the variation of the elements of the working capital the following logic is used:

- In the case of an active element, the growth has a negative influence upon the treasury, while a diminishing of this has a positive influence;
- In the case of a passive element, the judging is in opposition.

Although the IAS 7 Norm recommends the use of the direct method, especially to satisfy the informational needs of the investors (that can proceed to the estimation of the future treasury flows and of the dividends that could be cashed in on future periods), many companies prefer to use the indirect method, due to the its accordance with an engagement accounting.

The general presentation manner of the treasury flows overview is suggested by the following scheme:

The treasury flows relative to the exploitation activities

No matter if we use the direct or indirect method, the final information is:

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- I. The net treasury flow from exploitation activities;

The treasury flows relative to the investments activities

The companies use only incomings and payments type information.

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- II. The net treasury flow from investments activities;

The treasury flows relative to the financing activities

The companies use only incomings and payments type information.

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- III. The net treasury flow from financing activities;
IV. The net variation of the liquidities and liquidity equivalent;
V. The effect of the variation of foreign currencies exchange rates;
VI. The liquidities and liquidity equivalent at the beginning of the exercise (according to the balance);
VII. The liquidities and the liquidity equivalent at the end of the exercise (VI + IV + V).

Conclusions through examples:

1. You have the following information: Incomings from the clients 200 000 lei; payments towards the suppliers 15 000 lei; payments towards the employees 2 500 lei; interests paid in connection with the exploitation activity 100 lei; tax upon profit paid 6 000 lei; payments regarding: land acquisitions 100 000 lei; installations acquisitions 400 000 lei; incomings from the sale of equipments 50 000 lei; cashed in dividends 120 000 lei; incomes from the emission of social capital cashed in 7 000 lei; incomings from long term loans 1 500 lei. According to IAS 7, which are the sizes of the cash flows from exploitation activities, investments and financing activities?

Solution:

Exploitation flow	Investments flow	Financing flow
+ cashing in from the clients 200 000	– payments for land acquisitions 100 000	+ incomes from capital emissions 7 000
– payments towards suppliers 15 000	– payments for installations acquisitions 400 000	+ incomings from long term loans 1 500
– payments towards employees 2 500	+ incomings from the sale of equipments 50 000	
– interests paid connected to exploitation 100	+ cashed in dividends 120 000	
– tax upon profit paid 6 000		
= +176 400 lei	= –330 000 lei	= + 8 500 lei

2. You have the following information: profit before tax 25 000 lei; redemption expenses 1 700 lei; losses from foreign currency exchange rates differences 1 200 lei; incomes from financial investments 3 600 lei; clients: initial balance 4 000 lei – final balance 4 600 lei; stocks: initial balance 7 00 lei – final balance 1 500 lei; suppliers: initial balance 4 666 lei – final balance 3 500 lei; paid exploitation interests 1 200 lei; paid exploitation interests 1 200 lei; paid profit tax 1 400

lei; cashed insurance 200 lei. According to IAS 7, which is the size of the cash flow from the exploitation activity?

Solution:

Profit before tax	25 000
+ redemption expenses	+ 1 700
+ losses from foreign currency exchange rates differences	+ 1 200
– incomes from financial investments	– 3 600
– increase of debts towards the clients	– 600
+ decrease of stocks	+ 5 500
– decrease of suppliers	– 1 100
– paid interests	– 1 200
– paid profit tax	– 1 400
+ cashed insurance	+ 200
= Cash flow from the exploitation activity	+ 25 700

3. You have the following information: profit before tax 33 500 lei; redemption expenses 750 lei; clients: initial balance 2 000 lei – final balance 600 lei; stocks: initial balance 3 000 lei – final balance 3 900 lei; suppliers: initial balance 6 000 lei – final balance 8 400 lei; paid profit tax 300 lei. The expenses with interest have been in the sum of 1 000 lei, out of which 425 lei have been paid within the period. Other 250 lei connected to the interest expenses for the previous period were also paid during this period. 350 lei have been cashed in from capital emissions and other 325 lei from long term loans. There were made payments for the acquisition of a land valued at 2 550 lei and there were cashed in 2 300 lei from the sale of an installation. According to IAS 7 which are the sizes of the exploitation flows, investments and financing generated by these operations?

Solution:

Exploitation flow	Investments flow	Financing flow
+ profit before the taxation 33 500	– payments for lands acquisition 2 550	+ incomings from capital issues 350
+ depreciation expenses 750	+ incomings from selling equipments 2 300	+ incomings from long term loans 325

Exploitation flow	Investments flow	Financing flow
+ diminishing the clients claims 1 400		
– increases of stocks 900		
+ increases of debts suppliers 2 400		
– taxation on paid profit 300		
+ expenses with the interest 1 000		
– paid interest 425		
– interest afferent to the previous paid time interval 250		
= + 37 175 lei	= -250	= + 675

4. What is the size of the value adjustment of the tangible and intangible fixed assets, knowing the following elements: expenses with compensations, donations and abandoned assets 5 000 lei; incomings from the selling of the assets and other capital operations 7 000 lei; incomings from adjustments for the depreciation of the circulating assets 8 000 lei; incomings from reactivated claims 2 000 lei; incomings from adjustments for the depreciation of the financial fixed assets 5 000 lei; incomings from adjustments for the depreciation of the tangible fixed assets 800 lei; expenses with the fixed assets amortization 2 000 lei.

Solution: Adjustment = expenses – incomes = 2 000 – 800 = 1 200 lei.

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ABSTRACT

The balance sheet presents the liquidities balance and the liquidity equivalents of the company at the end of the period. By examining the balances referring to the two consecutive periods, it can be stated that if the liquidities and the liquidity equivalents have increased or have decreased during the period. But the balance does not indicate why these balances have varied during the exercise. The profit and loss balance presents the information related to incomes, expenses and the results due to the different activities – key-points regarding the sources and the use of the liquidities and the liquidity equivalents, but this financial situation does not explain why the respective elements have increased or decreased. Even further, not on fewer occasions behind some significant profits, the profit and loss balance can hide serious treasury problems of the company.

Key words: Treasury Flows; Painting Flows; Balance Sheet; Liquidity.

JEL classification: M41.