FINANCIAL IMPLICATIONS OF THE IAS/IFRS ADOPTION ON THE CIRCULATING ELEMENTS OF THE LIQUID ASSETS TYPE

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Within this article one presents some aspects regarding the affectation of the liquid assets both in leu and in currency by the International Standards of Financial Reporting. Regarding the liquid assets in currency we gave some precisions related to their presentation within the financial situations, and regarding the liquid assets in leu we made some appreciations regarding the synthesis document – the situations of the treasury flows.

Key words: cash-flow, transactions in currency, non-monetary elements, monetary elements, cash equivalent

Since the 1st of January 1999, the beginning of the coming into force of the Economic and Monetary Union (EMU), euro has become a currency with its own rights, and the exchange rates between the euro and the national participating currencies have been irrevocably established, i.e. the risk of the subsequent exchange differences of these currencies being eliminated starting with this date. IAS 21 Requirements – The effects of the exchange rates variation, regarding the conversion of the transactions in currency and the financial situations of the operations abroad must be strictly applied to the passing to the euro. The same reasoning is applied to the exchange currency rates when the countries adhere to the EMU in the subsequent stages.

This means that, especially:

- the assets and the monetary debts in currency resulting from transactions will continue to be converted in the functional currency on the closing rate. Any differences of the resulting exchange rates will be immediately recognized as incomes or expenses, excepting the case in which an entity will continue the applications of its accounting policies existing for the gains and losses relative to the covering of the exchange rate risk in case of a forecast transaction ;
- the differences of cumulated exchange rates afferent to the conversion of the financial situations for the operations abroad will be further classified as stockholders' equity and will be recognized as incomes or expenses only in what regards the giving up to the net investment in the operation abroad;
- the differences of the exchange rates resulted from the conversion of the debts expressed in the participating currencies won't be included in the accounting value of the afferent assets.

IAS 21 – The effects of the exchange rates require that the monetary elements of the currencies (as they are defined here) should be reported using the closing exchange rate on each date of the balance-sheet. As we mentioned above, the differences of the exchange rate which appeared in the conversion of the monetary elements must be recognized, in general, as incomes or expenses in the period in which they appear.

The beginning of the coming into force of the EMU after the date of the balance sheet does not modify the application of these requirements on the balance sheet data. According to IAS 10 –The events subsequent to the balance sheet date , it is not relevant if the closing exchange rate can fluctuate or not after the date of the balance sheet.

On the basis of *the treasury flow situation* one can make appreciations by the users regarding the capacity of the enterprise to generate cash and cash equivalent, the necessities of using the treasury flows. When it is used with the rest of the financial situations, the situation of the treasury flows provides information which permits the users to evaluate the modifications in the net assets of an entity, its financial structure (inclusively its liquidity and solvability), as well as the capacity of the enterprise of influencing the value and the moment of the treasury flows apparition, in the view to adapting to the ever changing circumstances and opportunities.

The information referring to the treasury flows are useful for the establishment of an entity capacity of generating cash and cash equivalent and give the possibility to the users of developing models of evaluation and comparison of the updated value of the future treasury flows belonging to different entities. Also, this information raises the degree of comparativeness of the results reporting form exploiting between different entities, since they eliminate the effects of using different accounting treatments for the dsmr transactions and events.

The information referring to the treasury flows is often used as an indicator of the value, the apparition moment and of the certitude of the future treasury flows. This is very useful in checking the exactitude of the former evaluations of the future treasury flows, as well as in examining the relationships between profitability and treasury net flows, and of the impact of price modification.

The cash equivalents are detained more with the view to fulfilling the liabilities in cash on a short term, than for investments or on other purposes. To classify a placement as a cash equivalent, this one must be easily convertible in a cash pre-established sum and to be subject to an insignificant risk of changing the value.

Consequently, an investment is normally qualified as a cash equivalent only when it has a low maturity, for let's say three months or less since the date of purchasing. Investments in the shareholders' equity are not considered cash equivalents, excepting the case when they are in their economic fund, cash equivalents, for instance in the case of the preferred stocks during a short period before their falling due and with a date of specified compensation.

Generally the bank loans are considered financing activities. Anyway, in certain countries, the overdrafts which are reimbursable at sight make an integrant part form the management of entity cash. In these circumstances, the overdrafts are considered a component of the cash and cash equivalent. A characteristic of these banking arrangements is the fact the sold frequently fluctuates between positive and negative.

The treasury flows exclude the movements between the elements which constitute cash or cash equivalents, because these components are part of the cash management of an entity, and not from the activities of operation, investment and financing. The management of the cash presupposes the placement of the cash surplus in cash equivalents.

An entity presents its treasury flows from the activities of operation, investment and financing in a manner which correspond best to its activity. The classification on activities provide information that allow the users to establish the impact of the respective activities on the financial position of the entity, as well as the value of the cash and cash equivalent. This information can also be used, to evaluate the relations that appear between the respective activities.

A single transaction can include treasury flows that are differently classified. For example, when the reimbursement in cash of a loan includes both the interest and the borrowed capital, the interest element can be classified as an operation activity, and the capital element, as a financing activity.

The value of the treasury flows which come from activities of operation is a key-indicator of the measure in which the activities of the entity generated sufficient treasury flows in order to repay the loans, to maintain the capacity of functioning of the entity, to pay dividends and to make new investments, without resorting to external financing sources. The information regarding the specific components of the treasury flows from operations, together with other information, are useful in the forecasting of the future treasury flows from operations.

The treasury flows coming from operation activities are derived, in the first place from the main income producing activities of the entity. As a consequence, they result, in general, from the transactions and other events which enter into the determination of the profit or of the loss.

The separate presentation of the treasury flows coming from investment activities is important because the treasury flows represent the extent to which the expenses served to the obtaining of the resources meant to generate future earnings and treasury flows. The separate presentation of the treasury flows coming from financing activities is important because it is useful in predicting the future treasury flows expected by the financers of the entity.

The treasury flows coming from the transaction effectuated in currency will be recorded in the functional currency of an entity through the application of the exchange rate between the functional currency and the currency, on the value in currency, on the date of the treasury flow. For the treasury flows afferent to a branch abroad will be converted on the exchange rate between the functional currency and the currency, on the date of the treasury flow.

The unachieved profit and losses that come from the variation of the currency exchange rate are not treasury flows. Anyway, the effect of the variation of the currency exchange rate on the cash and the cash equivalents, detained or owed in currency is reported in the situation of the treasury flows in order to reconcile the cash and the cash equivalents at the beginning and at the end of the period. This value is presented separately from the treasury flows coming from activities of operation, investments, financing and includes the differences, if they exist, of those treasury flows which were reported to the exchange rate at the end of the period.

In the case of the interests and dividends cashed or paid, the treasury flows will be presented separately. Each of these ones will be classified in a consequent manner from a period to another, as being generated either by operation activities or investment or financing. Both the paid interest and the cashed interest and dividends are classified by the financial institutions as treasury flows form operations.

Anyway, there is no consensus regarding the classification of these treasury flows by other entities. Both the paid interest, and the cashed interest and the dividends can be classified as treasury flows from operations, because they enter into the determination of the profit or of the loss. Alternatively, the paid interest and the cashed interest and dividends can be classified as treasury flows from financing and respectively from investment, because they represent costs of the attraction of the financing sources or of the investments.

The paid dividends can be classified as treasury flows from financing, because they represent cost of the attracting the financing resources. Alternatively, the paid dividends can be classified as a component of the treasury flow from activities of operation in order to help the users to determine the capacity of an entity of paying dividends from treasury flows of operation.

The treasury flows coming from the profit tax will be presented separately and will be classified as treasury flows from operation activities, with the exception of the situation in which they can be allocated specifically to the activities of financing and investment.

The separate presentation of the treasury flows which represent increases of the capacity of operation and of treasury flows necessary to the maintenance of the capacity of operation is useful, offering the possibility to the users to determine if the entity invests adequately for the maintenance of the operation activity. An entity which does not invest adequately in the maintaining of its operation capacity can prejudice its profitability in the future for the current liquidity and the allocations towards shareholders.

In a hyperinflationist economy, the reporting without conversion of the results of operation and of the financial position in the local currency is not useful. The money loses its purchasing power to such an extent, so that the comparison of the sums that result from transactions and other events that took place at different moments, in the very moment of the same accounting period, induces in error. One didn’t establish an absolute rate from which level the hyperinflation is considered. The date of the moment on which the conversion of the financial situations becomes necessary is a problem of professional reasoning.

The hyperinflation is indicated by characteristics of the economic environment of a country, which include, but do not limit to the followings:

- most of the population prefers having the fortune in non-monetary assets or in a relatively stable currency, the sums detained in the local currency are immediately invested in order to maintain the purchasing power;
- most of the population appreciates the monetary values as compared to a relatively stable currency and not with the local currency, the prices can be expressed in the same currency;
- the sales and the purchases on credit are done on prices that compensate the expected loss of the purchasing power during the crediting period, even if the period is short;
- the interest rates, the wages and the prices are related by an index of prices;
- the accumulated rate of the inflation on three consecutive years gets close or exceeds 100%.

In most of the countries, the financial situations are drawn up on the basis of the historical cost, without considering the changes on the general level of the prices and the increase of the prices specific to the detained activities, excepting the case in which the corporal immobilizations and the financial investments can be reevaluated .

Some entities present anyway primary financial situations based on the method of the current cost, which reflect the effects of the price modifications specific to the detained activities. In a hyperinflationist economy, the financial situations based either on the historical cost model, or on the current cost one, are useful only if they are expressed as the unity of current measure since the date of the balance sheet.

The sums of the balance sheet which are not expressed as against the unity of the current measure on the balance sheet date are conversed through the application of a general index of the prices. The monetary elements are not conversed, since they are already expressed as against the current monetary unity on the balance sheet date. The monetary elements are the pecuniary reserves and the elements to cash or pay in money.

The assets and the liabilities bound through a contract of price modification, the way the bonds and loans are, which are indexed, are adjusted in conformity with the contract for establishing the basic value on the date of the balance sheet. These elements are recorded at this adjusted value in the converse balance sheet. All the other assets and liabilities are non-monetary. Some non-monetary elements are recorded at current values on the date of the balance sheet, as, for example, the net achievable value and the market value, so they are not conversed. All the other non-monetary assets and liabilities are conversed.

The most non-monetary elements are recorded at the cost or cost minus depreciation: consequently, they are expressed at current values on the purchasing date. The conversed cost or the cost minus depreciation conversed for each element is determined through the application of the historical cost. The conversed cost or the cost minus depreciation for each element is determined through the application of the historical cost and of the depreciation cumulated to the variation of a general index of the prices to the date of the balance sheet.

As a consequence, corporal immobilizations, financial investments, stocks of raw materials and goods, commercial fund, patent, trademarks and similar assets are conversed since the date of their buying. The products stocks in course of execution and of the finished products are conversed since the date of the apparition of costs of acquisitions and processing.

The conversing value of a non-monetary element is diminished in conformity with the requirements of the Standards, when it exceeds the recoverable value from the future utilization of the element (inclusively the selling or other form of giving up). That’s why, in such cases, the conversed values of the corporal immobilizations, the commercial fund, the patents and the trademarks are diminished at the recoverable value, the conversed values of the stocks are diminished at the net achievable value, and the conversed values of the short term investments are diminished till the market value.

The impact of inflation is usually acknowledged in the costs of the leverage. The conversion is inadequate during the same period of capital expenses financed through borrowings and of the capitalizations of the part of the leverage costs which compensate inflation, during the same period. This part of the costs of leverage is acknowledged as an expense in the period in which the costs were supported.

In an inflation period, an entity which detains a surplus of monetary assets compared to the monetary debts loses purchasing power, and an entity with a surplus of monetary debts as compared to the monetary assets gains purchasing power, if the assets and the debts are not related to a level of prices. The gain or the loss of the net monetary position can derive as a difference resulted from the correction of the non-monetary assets, the shareholders’ equity and the elements of the profit and loss account, and of the adjusting of the assets and debts related by an index. The gain or the loss can be estimated through the application of a general index of the prices to the average of the difference between the assets and the monetary debts of the respective periods.

The gain or the loss of the net monetary position is included in the net income. The adjusting of the respective assets and debts bound through a contract by the variation of the prices is compensated with the gain or the loss of the net monetary position. Other elements from the profit and loss account, such as the incomes and the expenses from the interests and the exchange rate differences afferent to the invested or borrowed funds are, also associated with the net monetary position. Although such elements are separately presented, the presentation in the profit and loss account can be useful, together with the gain and loss of the net monetary position.

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