What is so important about a **Statement of Cash Flows**?

Statement of Cash Flows is a mandatory part of a company’s financial report since 1987.

Statement of Financial Accounting Standards No. 95

Cash is King in Business, the statement organizes the flow of cash and it is an important tool for key decision makers. A Statement of Cash Flows will allow companies to see the inflow and outflow of Cash. Most companies use the indirect method to consolidate their Statement of Cash Flows. The Statement is divided into **Operating**, **Investing** and **Financing Activities.**

**Sample of a Basic Cash Flow Statement:**

**Statement of Cash Flows**

**Green Company**

**FY Ended December 31, 2011**

**Cash Flow From Operations:**

**Net Income *$2,000,000***

***Addition to Cash***

*Depreciation**10,000*

Decrease in A/R15,000

Increase in A/P15,000

Increase in Taxes Payable2,000

**Subtraction from Cash**

Increase in Inventory(30,000)

**Net Cash From Operations $2,012,000**

**Cash Flow From Investing:**

Purchase Equipment(500,000)

**Cash Flow From Financing:**

Notes Payable (Sold a Bond)10,000

**Cash Flow for FY Ended 12/31/2011 $1,522,000**

**Operations**

**Measuring the cash inflows and outflows caused by core business operations, the operations component of cash flow reflects how much cash is generated from a company's products or services. Generally, changes made in cash, accounts receivable, depreciation, inventory and accounts payable are reflected in cash from operations.**

**Cash flow is calculated by making certain adjustments to net income by adding or subtracting differences in revenue, expenses and credit transactions (appearing on the balance sheet and income statement) resulting from transactions that occur from one period to the next. These adjustments are made because non-cash items are calculated into net income (income statement) and total assets and liabilities (balance sheet). So, because not all transactions involve actual cash items, many items have to be re-evaluated when calculating cash flow from operations.**

**Investing**

**Changes in equipment, assets or investments relate to cash from investing. Usually cash changes from investing are a "cash out" item, because cash is used to buy new equipment, buildings or short-term assets such as marketable securities. However, when a company divests of an asset, the transaction is considered "cash in" for calculating cash from investing.**

**Financing**

**Changes in debt, loans or dividends are accounted for in cash from financing. Changes in cash from financing are "cash in" when capital is raised, and they're "cash out" when dividends are paid. Thus, if a company issues a bond to the public, the company receives cash financing; however, when interest is paid to bondholders, the company is reducing its cash.**

**Conclusion**

**A company can use a cash flow statement to predict future cash flow, which helps with matters in budgeting. For investors, the cash flow reflects a company's financial health: basically, the more cash available for business operations, the better. However, this is not a hard and fast rule. Sometimes a negative cash flow results from a company's growth strategy in the form of expanding its operations.**

**By adjusting earnings, revenues, assets and liabilities, the investor can get a very clear picture of what some people consider the most important aspect of a company: how much cash it generates and, particularly, how much of that cash stems from core operations.**

**For further entertainment:**

**Summary of Statement No. 95**

**Statement of Cash Flows (Issued 11/87)**

**Summary**

**This Statement establishes standards for cash flow reporting. It supersedes APB Opinion No. 19, Reporting Changes in Financial Position, and requires a statement of cash flows as part of a full set of financial statements for all business enterprises in place of a statement of changes in financial position.**

**This Statement requires that a statement of cash flows classify cash receipts and payments according to whether they stem from operating, investing, or financing activities and provides definitions of each category.**

**This Statement encourages enterprises to report cash flows from operating activities directly by showing major classes of operating cash receipts and payments (the direct method). Enterprises that choose not to show operating cash receipts and payments are required to report the same amount of net cash flow from operating activities indirectly by adjusting net income to reconcile it to net cash flow from operating activities (the indirect or reconciliation method) by removing the effects of (a) all deferrals of past operating cash receipts and payments and all accruals of expected future operating cash receipts and payments and (b) all items that are included in net income that do not affect operating cash receipts and payments. If the direct method is used, a reconciliation of net income and net cash flow from operating activities is required to be provided in a separate schedule.**

**This Statement requires that a statement of cash flows report the reporting currency equivalent of foreign currency cash flows, using the current exchange rate at the time of the cash flows. The effect of exchange rate changes on cash held in foreign currencies is reported as a separate item in the reconciliation of beginning and ending balances of cash and cash equivalents.**

**This Statement requires that information about investing and financing activities not resulting in cash receipts or payments in the period be provided separately.**

**This Statement is effective for annual financial statements for fiscal years ending after July 15, 1988. Restatement of financial statements for earlier years provided for comparative purposes is encouraged but not required.**