SESSION 1: FINANCIAL ACCOUNTING AND REPORTING
DATE: FRIDAY, FEBRUARY 23
TIME: 1:45 – 3:15 PM

Go with the Flow: A Consistent Approach to the Statement of Cash Flows

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ABSTRACT: The required classification of cash flows as operating, investing, or financing (required by SFAS No. 95) is relatively straightforward. However, the classification of some items has generated considerable debate. We believe that most classification issues can be resolved by reference to the income statement. Conceptually, the operating section of the statement of cash flows (SCF) should include the cash flows for items that are properly included as a component of operating income on the income statement. Thus, "cash flow from operations" should be consistent with "income from operations," except that it is measured using the cash basis instead of the accrual basis.

Suggested changes to the current format for the SCF include: 1) cash interest earned should be included in the investing section, 2) cash interest paid should be included in the financing section, and 3) cash paid for operating assets should be included in the operating section. Finally, since it usually is not possible to relate cash paid for taxes to specific items, cash paid for taxes should be shown separately in the SCF after the financing section and immediately preceding the net increase or decrease in cash. Cash flows for all items not included in operating income would be classified as either investing or financing cash flows. These changes should improve financial reporting by clarifying what is included in the operating section of the SCF and increasing the consistency between the SCF and the income statement.