

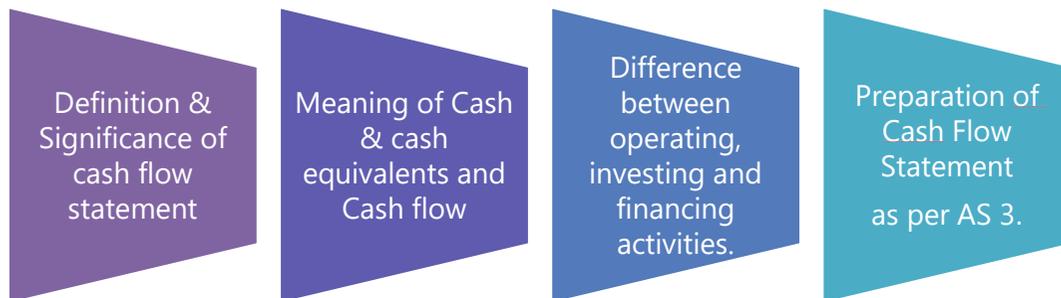
UNIT 2: CASH FLOW STATEMENTS

LEARNING OUTCOMES

After studying this unit, you will be able to–

- ◆ Define cash flow statement as per AS 3 “Cash Flow Statements”.
- ◆ Differentiate operating, investing and financing activities.
- ◆ Learn the various elements of cash and cash equivalents.
- ◆ Prepare cash flow statement both by direct method and indirect method.

UNIT OVERVIEW

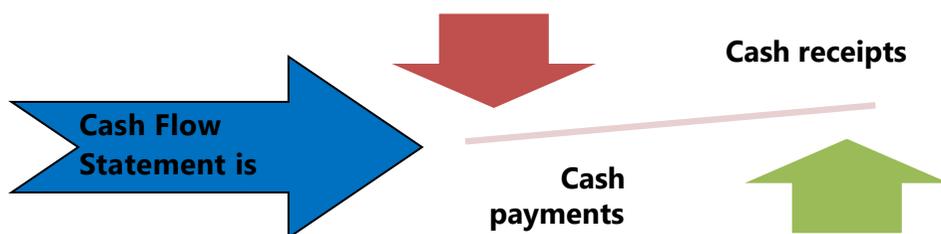


2.1 INTRODUCTION

Information about the cash flows of an enterprise is useful in providing users of financial statements with a basis to assess the ability of the enterprise to generate cash and cash equivalents and the needs of the enterprise to utilise those cash flows. The economic decisions that are taken by users require an evaluation of the ability of an enterprise to generate cash and cash equivalents and the timing and certainty of their generation.

The Standard deals with the provision of information about the historical changes in cash and cash equivalents of an enterprise by means of a cash flow statement which classifies cash flows during the period from operating, investing and financing activities.

This statement provides relevant information in assessing a company's liquidity, quality of earnings and solvency.



Benefits:

- (a) Cash flow statement provides information about the changes in cash and cash equivalents of an enterprise.
- (b) Identifies cash generated from trading operations.
- (c) The operating cash surplus which can be applied for investment in fixed assets.
- (d) Portion of cash from operations is used to pay dividend and tax and the other portion is ploughed back.
- (e) Very useful tool of planning.

Purpose:

Cash flow statements are prepared to explain the cash movements between two points of time.

Sources of Cash:

1. Issue of shares and debentures and raising long-term loan.
2. Sale of investments and other fixed assets.
3. Cash from operations (Net Operating Profit).

Applications of Cash

1. Redemption of preference shares and debentures and repayment of long-term loan.

2. Purchase of investments and other fixed assets.
3. Payment of tax.
4. Payment of dividend.
5. Loss on Operation (Net Operating Loss)

Note: Cash includes Bank Account also. Increase in cash or decrease in cash is put in the applications and the sources respectively just to balance the cash flow statement. At this juncture, you may note that changes in all balance sheet items are to be taken into consideration separately in cash flow statement for explaining movement of cash.

2.2 ELEMENTS OF CASH

As per AS 3, issued by the Council of the ICAI,

'Cash' include:

- (a) Cash in hand,
- (b) Demand deposits with banks, and

Cash equivalents include:

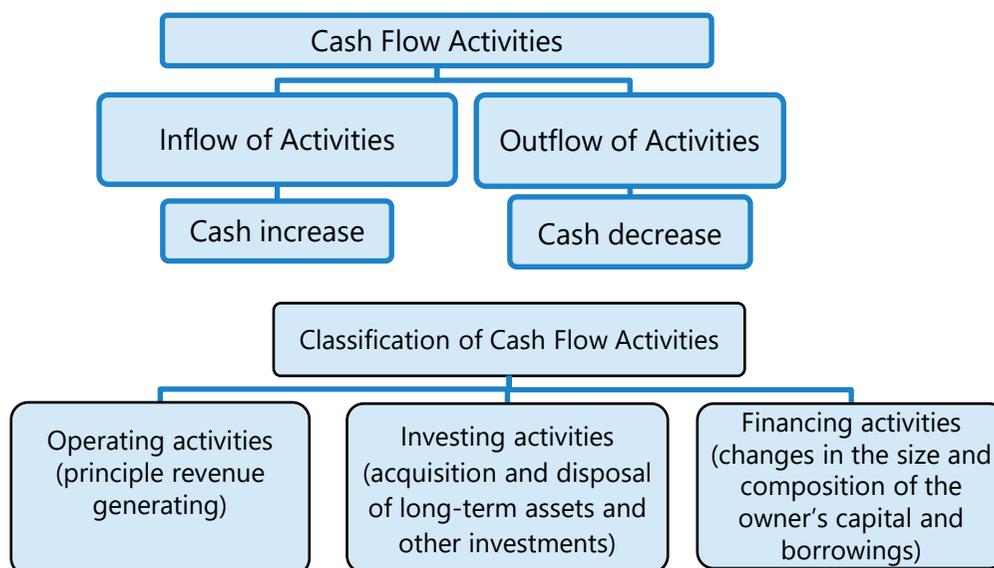
- (a) Components
 - Short term highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value
 - Securities with short maturity period of, say, three months or less from the date of acquisition
- (b) Objective
 - Deploy, for a short period, idle cash required to meet short-term cash-commitments.
- (c) Examples
 - Acquisition of preference shares, shortly before their specified redemption date, bank deposits with short maturity period, etc.

Conclusion: Thus, cash flow statement deals with flow of cash funds but does not consider the movements among cash, bank balance payable on demand and

investment of excess cash in cash equivalents. Examples are cash withdrawn from current account, cash deposited in bank for 60 days, etc.

2.3 CLASSIFICATION OF CASH FLOW ACTIVITIES

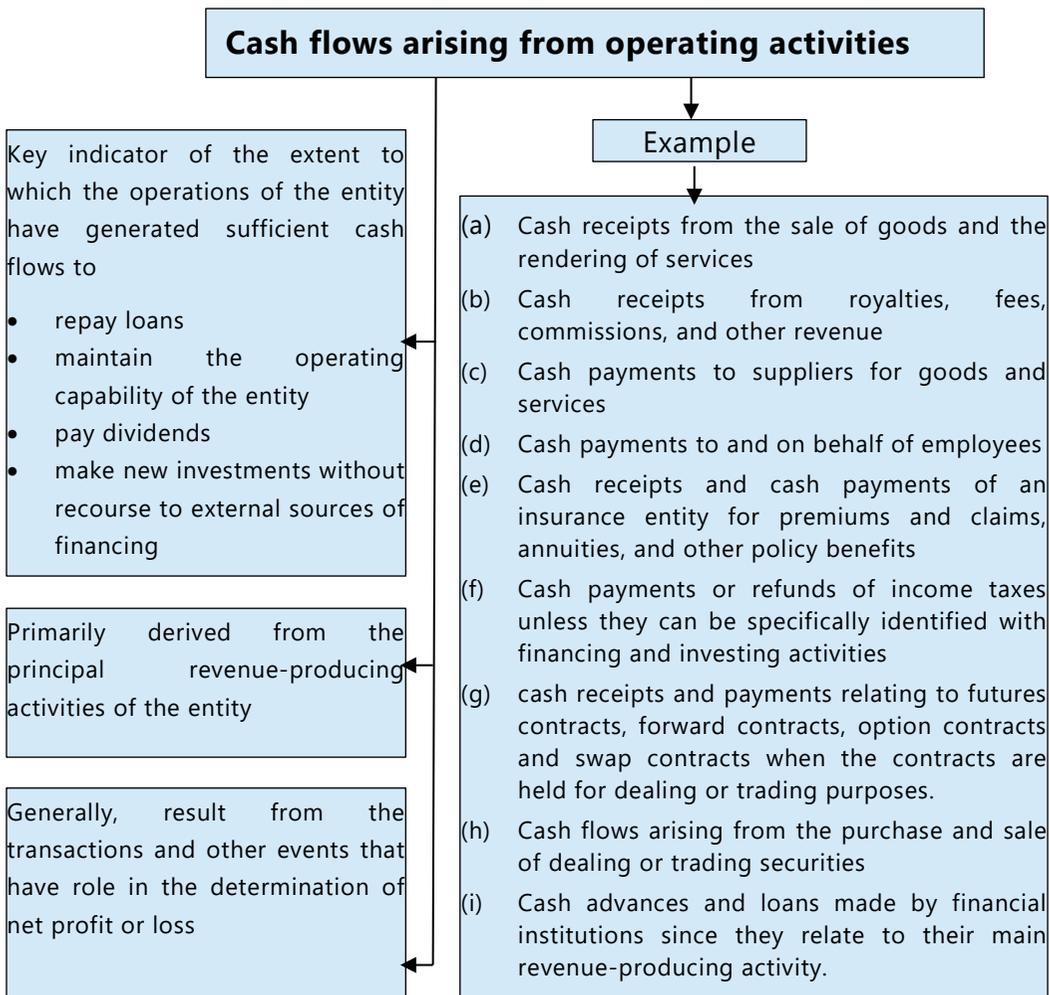
AS 3 provides explanation for changes in cash position of the business entity. As per Accounting Standard 3, cash flows during the period are classified as Operating; Investing and Financing activities.



2.3.1 Operating Activities

1. *Definition:* These are the principal revenue generating activities of the enterprise.
2. *Net Impact:* Net impact of operating activities on flow of cash is reported as 'Cash flows from operating activities' or 'cash from operations'.
3. *Key Indicator:* The amount of cash flows from operating activities is a key indicator of the extent to which the operations of the enterprises have generated sufficient cash flows to:
 - (a) Maintain the operating capability of the enterprise;
 - (b) Pay dividends, repay loans; and

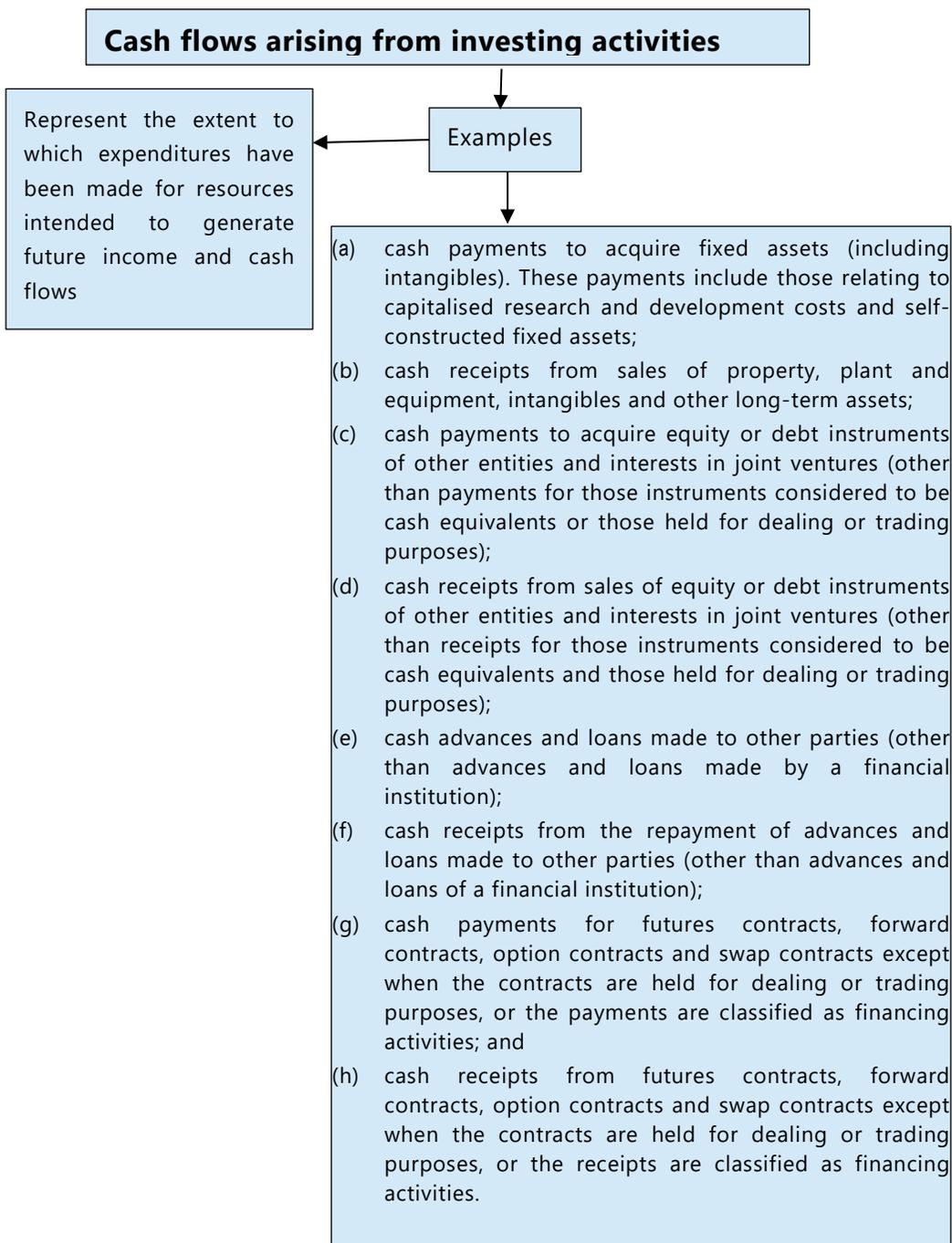
- (c) Make new investments without recourse to external sources of financing.
4. *Information Provided:* It provides useful information about financing through working capital.
5. *Benefits:* Information about the specific components of historical operating cash flows is useful, in conjunction with other information, in forecasting future operating cash flows.



2.3.2 Investing activities

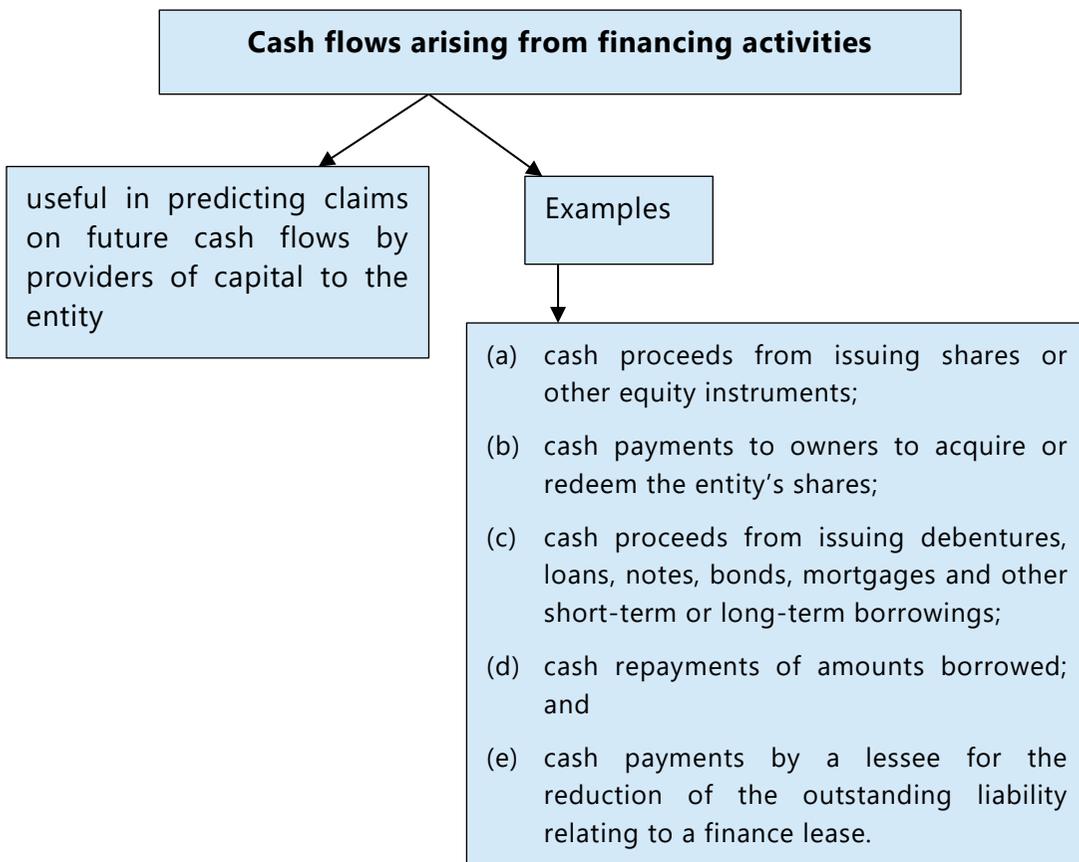
1. *Definition:* These are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

2. *Separate Disclosure*: Separate disclosure of cash flows arising from investing activities is important because the cash flows represent the extent to which the expenditures have been made for resources intended to generate future incomes and cash flows.



2.3.3 Financing activities

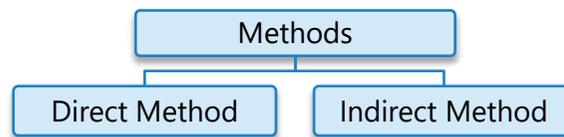
1. *Definition:* These are the activities that result in changes in the size and composition of the owner's capital (including preference share capital) and borrowings of the enterprise.
2. *Separate Disclosure:* The separate disclosure of cash flows arising from financing activities is important because it is useful in predicting claims on future cash flows by providers of funds (both capital and borrowings) to the enterprise.





2.4 CALCULATION OF CASH FLOWS FROM OPERATING ACTIVITIES

1. *Components:* Cash flows from operating activities result from the transactions and other events that enter into the determination of net profit or loss.
2. *Methods:* An enterprise can determine cash flows from operating activities using either:



- (a) **Direct Method:** The direct method, whereby major classes of gross cash receipts and gross cash payments are considered; or
- (b) **Indirect Method:** The indirect method, whereby net profit or loss is adjusted for the effects of transactions of a non-cash nature, deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing activities.

2.4.1 Direct Method

1. Information Required

- (a) Gross receipts and gross cash payments may be obtained from the accounting records to ascertain cash flows from operating activities.
- (b) For example,
 - (i) information about cash received from trade receivables,
 - (ii) payment to trade payables, cash expenses etc., which may be obtained by an analysis of cash book.
- (c) In actual practice, the relevant information is obtained by adjusting sales, cost of sales and other items in the profit and loss accounts for:
 - Changes during the period in inventories and operating receivables and payables;
 - Other non-cash items such as depreciation on fixed assets,

goodwill written off, preliminary expenses written off, loss or gain on sale of fixed assets etc.; and

- Other items for which the cash effects are investing or financing cash flows. Examples are interest received and paid, dividend received and paid etc., which are related to financing or investing activities and are shown separately in the cash flow statement.
2. The direct method provides information which may be useful in estimating future cash flows and which is not available under the indirect method and is, therefore, considered more appropriate than the indirect method.
 3. However, indirect method of determining the cash from operating activities is more popular in actual practice.

2.4.2 Indirect Method

Under the indirect method, the net cash from operating activities is determined by adjusting net profit or loss instead of individual items appearing in the profit and loss account. Net profit or loss is also adjusted for the effect of:

- (a) changes during the period in inventories and operating receivables and payables;
- (b) non-cash items such as depreciation; and
- (c) all other items for which the cash effects are financing or investing cash flows.

2.4.3 Conclusion

1. It is worth noting that both direct and indirect methods adjust current assets and current liabilities related to operating activities to determine cash from operating activities.
2. But direct method adjust individual items of profit and loss account and indirect method adjusts overall net profit (or loss) to determine cash from operation.
3. Therefore, indirect method fails to provide break-up of cash from operations.

Proforma of 'Cash Flow from Operating Activities' by indirect method

			₹
Net Profit for the year			-
<i>Add:</i> Non-Cash and Non-Operating Expenses:		-	
	Depreciation	-	
	Loss on Sale of Assets	-	
	Provision for taxation, etc.	-	
<i>Less:</i> Non-Cash and Non-Operating Incomes:			
	Profit on Sale of Assets	-	
Net Profit after Adjustment for Non-Cash Items			(-)
Cash from operation	=	Net Profit (after adjustment for Non-cash Items)	
	-	Increase in Current Assets	
	+	Decrease in Current Assets	
	+	Increase in Current Liabilities	
	-	Decrease in Current Liabilities	



2.5 CALCULATION OF CASH FLOWS FROM INVESTING ACTIVITIES

1. These activities are related to the acquisition and disposal of long-term assets, non-operating current assets and investments which results in outflow of cash.
2. Disposal of the aforesaid assets results in inflow of cash.
3. Thus, inflows and outflows related to acquisition and disposal of assets, other than those related to operating activities, are shown under this category.



2.6 CALCULATION OF CASH FLOWS FROM FINANCING ACTIVITIES

1. These activities are basically related to the changes in capital and borrowing of the enterprise which affect flow of cash.

2. Redemption of shares and repayment of borrowings results in outflow of cash.
3. Thus inflows and outflows related to the amount of capital and borrowings of the enterprise are shown under this head.

Note: Students are advised to refer full text of Accounting Standard on Cash Flow Statements (AS 3) for the better understanding of the chapter.

2.7 ILLUSTRATIONS

Illustration 1

Intelligent Ltd., a non-financial company has the following entries in its Bank Account. It has sought your advice on the treatment of the same for preparing Cash Flow Statement.

- (i) *Loans and Advances given to the following and interest earned on them:*
 - (1) *to suppliers*
 - (2) *to employees*
 - (3) *to its subsidiaries companies*
- (ii) *Investment made in subsidiary Smart Ltd. and dividend received*
- (iii) *Dividend paid for the year*
- (iv) *TDS on interest income earned on investments made*
- (v) *TDS on interest earned on advance given to suppliers*
- (vi) *Insurance claim received against loss of fixed asset by fire*

Discuss in the context of AS 3 Cash Flow Statement.

Solution

- (i) **Loans and advances given and interest earned**

(1) to suppliers	Operating Cash flow
(2) to employees	Operating Cash flow
(3) to its subsidiary companies	Investing Cash flow

(ii) **Investment made in subsidiary company and dividend received**

Investing Cash flow

(iii) **Dividend paid for the year**

Financing Cash Outflow

(iv) **TDS on interest income earned on investments made**

Investing Cash Outflow

(v) **TDS on interest earned on advance given to suppliers**

Operating Cash Outflow

(vi) **Insurance claim received of amount loss of fixed asset by fire**

Extraordinary item to be shown under a separate heading as 'Cash inflow from investing activities'.

Illustration 2

Following are extracts of the Balance Sheets of Ajay Ltd.:

	Particulars	Notes	31.3.20X1 ₹	31.3.20X2 ₹
	Equity and Liabilities			
	Shareholder's funds			
(a)	Share capital	1	5,00,000	5,00,000
(b)	Reserve & surplus	2	50,000	90,000
	Non-current liabilities			
(a)	Long-term borrowings	3	5,00,000	7,50,000
	Current liabilities			
(a)	Other current liabilities	4	---	5,000
	Assets			
	Non-current assets			
(a)	Intangible assets	5	2,05,000	1,80,000

Notes to accounts

		31.3.20X1	31.3.20X2
		₹	₹
1	Share Capital 50,000 Equity Shares of ₹10 each	5,00,000	5,00,000
2	Reserve & surplus Profit & Loss A/c	50,000	90,000
3	Long-term borrowings 10% Debentures	5,00,000	7,50,000
4	Other current liabilities Unpaid interest	---	5,000
5	Intangible assets Goodwill	2,05,000	1,80,000

You are required to show the related items in Cash Flow Statement.

Solution**An Extract of Cash Flow Statement for the year ending 31.3.20X2**

	₹
Cash flows from operating activities:	
Closing balance as per Profit & Loss A/c	90,000
Less: Opening balance as per Profit & Loss Alc	(50,000)
Add: Goodwill amortisation	25,000
Add: Interest on Debentures (Refer Note 1)	75,000
Net Cash from Operating Activities	1,40,000

Note 1 : Interest has been computed on the closing balance of debentures as on 31.3.20X2 assuming that all the additions/ deletions were made, if any, at the beginning of the year.

Cash flows from financing activities:

Proceeds from debentures (Refer Working Note)	2,50,000
Interest paid on Debentures [less unpaid]	(70,000)
Net Cash from Financing Activities	1,80,000

Working Note:

10% Debentures Account

<i>Particulars</i>	₹	<i>Particular</i>	₹
To Balance c/d	7,50,000	By Balance b/d	5,00,000
		By Bank A/c (Bal. fig.)	2,50,000
	7,50,000		7,50,000

Illustration 3

From the following information, calculate cash flow from operating activities:

Summary of Cash Account for the year ended March 31, 20X1

<i>Particulars</i>	₹	<i>Particulars</i>	₹
To Balance b/d	1,00,000	By Cash Purchases	1,20,000
To Cash sales	1,40,000	By Trade payables	1,57,000
To Trade receivables	1,75,000	By Office & Selling Expenses	75,000
To Trade Commission	50,000	By Income Tax	30,000
To Sale of Investment	30,000	By Investment	25,000
To Loan from Bank	1,00,000	By Repayment of Loan	75,000
To Interest & Dividend	1,000	By Interest on loan	10,000
		By Balance c/d	1,04,000
	5,96,000		5,96,000

Solution

Cash Flow Statement of
for the year ended March 31, 20X1(Direct Method)

Particulars	₹	₹
Operating Activities:		
Cash received from sale of goods	1,40,000	
Cash received from Trade receivables	1,75,000	
Trade Commission received	50,000	3,65,000
Less: Payment for Cash Purchases	1,20,000	
Payment to Trade payables	1,57,000	
Office and Selling Expenses	75,000	
Payment for Income Tax	30,000	(3,82,000)
Net Cash Flow used in Operating Activities		(17,000)

Illustration 4

The following summary cash account has been extracted from the company's accounting records:

Summary Cash Account

		(₹'000)
<i>Balance at 1.3.20X1</i>		35
<i>Receipts from customers</i>		2,783
<i>Issue of shares</i>		300
<i>Sale of fixed assets</i>		128
		3,246
<i>Payments to suppliers</i>	2,047	
<i>Payments for property, plant & equipment</i>	230	
<i>Payments for overheads</i>	115	

<i>Wages and salaries</i>	69	
<i>Taxation</i>	243	
<i>Dividends</i>	80	
<i>Repayments of bank loan</i>	250	(3,034)
<i>Balance at 31.3.20X2</i>		212

Prepare Cash Flow Statement of this company Hills Ltd. for the year ended 31st March, 20X2 in accordance with AS-3 (Revised).

The company does not have any cash equivalents.

Solution

Hills Ltd.

Cash Flow Statement for the year ended 31st March, 20X2 (Using direct method)

		(₹'000)
Cash flows from operating activities		
Cash receipts from customers	2,783	
Cash payments to suppliers	(2,047)	
Cash paid to employees	(69)	
Other cash payments (for overheads)	(115)	
Cash generated from operations	552	
Income taxes paid	(243)	
<i>Net cash from operating activities</i>		309
Cash flows from investing activities		
Payments for purchase of fixed assets	(230)	
Proceeds from sale of fixed assets	128	
<i>Net cash used in investing activities</i>		(102)

Cash flows from financing activities		
Proceeds from issuance of share capital	300	
Bank loan repaid	(250)	
Dividend paid	(80)	
<i>Net cash used in financing activities</i>		(30)
Net increase in cash and cash equivalents		177
Cash and cash equivalents at beginning of period		35
Cash and cash equivalents at end of period		212

Illustration 5

Prepare cash flow statement of M/s MNT Ltd. for the year ended 31st March, 20X1 with the help of the following information:

- (1) Company sold goods for cash only.
- (2) Gross Profit Ratio was 30% for the year, gross profit amounts to ₹ 3,82,500.
- (3) Opening inventory was lesser than closing inventory by ₹ 35,000.
- (4) Wages paid during the year ₹ 4,92,500.
- (5) Office and selling expenses paid during the year ₹ 75,000.
- (6) Dividend paid during the year ₹ 30,000.
- (7) Bank loan repaid during the year ₹ 2,15,000 (included interest ₹ 15,000).
- (8) Trade payables on 31st March, 20X0 exceed the balance on 31st March, 20X1 by ₹ 25,000.
- (9) Amount paid to trade payables during the year ₹ 4,60,000.
- (10) Tax paid during the year amounts to ₹ 65,000 (Provision for taxation as on 31.03.20X1 ₹ 45,000).
- (11) Investments of ₹ 7,00,000 sold during the year at a profit of ₹ 20,000.
- (12) Depreciation on fixed assets amounts to ₹ 85,000.
- (13) Plant and machinery purchased on 15th November, 20X0 for ₹ 2,50,000.
- (14) Cash and Cash Equivalents on 31st March, 20X0 ₹ 2,00,000.
- (15) Cash and Cash Equivalents on 31st March, 20X1 ₹ 6,07,500.

Solution

M/s MNT Ltd.
Cash Flow Statement for the year ended 31st March, 20X1
(Using direct method)

<i>Particulars</i>	₹	₹
<i>Cash flows from Operating Activities</i>		
Cash sales (₹ 3,82,500/.30)		12,75,000
Less: Cash payments for trade payables	(4,60,000)	
Wages Paid	(4,92,500)	
Office and selling expenses	(75,000)	(10,27,500)
Cash generated from operations before taxes		2,47,500
Income tax paid		(65,000)
Net cash generated from operating activities (A)		1,82,500
<i>Cash flows from investing activities</i>		
Sale of investments (7,00,000 + 20,000)	7,20,000	
Payments for purchase of Plant & machinery	(2,50,000)	
Net cash used in investing activities (B)		4,70,000
<i>Cash flows from financing activities</i>		
Bank loan repayment (including interest)	(2,15,000)	
Dividend paid	(30,000)	
Net cash used in financing activities (C)		(2,45,000)
Net increase in cash (A+B+C)		4,07,500
Cash and cash equivalents at beginning of the period		2,00,000
Cash and cash equivalents at end of the period		6,07,500

Illustration 6

Ryan Ltd provides you the following information at the year-end, March 31, 20X1:

	₹	₹
Sales		6,98,000
Cost of Goods Sold		(5,20,000)
		1,78,000
Operating Expenses (including Depreciation Expense of ₹ 37,000)		(1,47,000)
		31,000
Other Income / (Expenses):		
Interest Expense paid	(23,000)	
Interest Income received	6,000	
Gain on Sale of Investments	12,000	
Loss on Sale of Plant	(3,000)	
		(8,000)
		23,000
Income tax		(7,000)
		16,000

Information available:

	31st March 20X1	31st March 20X0
	₹	₹
Plant	7,15,000	5,05,000
Less: Accumulated Depreciation	(1,03,000)	(68,000)
	6,12,000	4,37,000

<i>Investments (Long term)</i>	1,15,000	1,27,000
<i>Inventory</i>	1,44,000	1,10,000
<i>Trade receivables</i>	47,000	55,000
<i>Cash</i>	46,000	15,000
<i>Prepaid expenses</i>	1,000	5,000
<i>Share Capital</i>	4,65,000	3,15,000
<i>Reserves and surplus</i>	1,40,000	1,32,000
<i>Bonds</i>	2,95,000	2,45,000
<i>Trade payables</i>	50,000	43,000
<i>Outstanding liabilities</i>	12,000	9,000
<i>Income taxes payable</i>	3,000	5,000

Analysis of selected accounts and transactions during 20X0-X1

1. *Purchased investments for ₹ 78,000.*
2. *Sold investments for ₹ 1,02,000. These investments cost ₹ 90,000.*
3. *Purchased plant assets for ₹ 1,20,000.*
4. *Sold plant assets that cost ₹10,000 with accumulated depreciation of ₹ 2,000 for ₹ 5,000.*
5. *Issued ₹ 1,00,000 of bonds at face value in an exchange for plant assets on 31st March, 20X1.*
6. *Repaid ₹ 50,000 of bonds at face value at maturity.*
7. *Issued 15,000 shares of ₹ 10 each.*
8. *Paid cash dividends ₹ 8,000.*

Prepare Cash Flow Statement as per AS-3 (Revised), using indirect method.

Solution

Ryan Ltd.
Cash Flow Statement
for the year ending 31st March, 20X1

	₹	₹
Cash flows from operating activities		
Net profit before taxation	23,000	
Adjustments for:		
Depreciation	37,000	
Gain on sale of investments	(12,000)	
Loss on sale of plant assets	3,000	
Interest expense	23,000	
Interest income	(6,000)	
Operating profit before working capital changes	68,000	
Decrease in trade receivables	8,000	
Increase in inventory	(34,000)	
Decrease in prepaid expenses	4,000	
Increase in trade payables	7,000	
Increase in outstanding liabilities	3,000	
Cash generated from operations	56,000	
Income taxes paid*	(9,000)	
<i>Net cash generated from operating activities</i>		47,000
Cash flows from investing activities		
Purchase of plant	(1,20,000)	
Sale of plant	5,000	
Purchase of investments	(78,000)	

Sale of investments	1,02,000	
Interest received	6,000	
<i>Net cash used in investing activities</i>		(85,000)
Cash flows from financing activities		
Proceeds from issuance of share capital	1,50,000	
Repayment of bonds	(50,000)	
Interest paid	(23,000)	
Dividends paid	(8,000)	
<i>Net cash from financing activities</i>		<u>69,000</u>
Net increase in cash and cash equivalents		31,000
Cash and cash equivalents at the beginning of the period		15,000
Cash and cash equivalents at the end of the period		<u>46,000</u>

Note: Significant non-cash adjustments: Issued ₹ 1,00,000 of bonds at face value for acquisition of plant on 31st March, 20X1.

***Working Note:**

	₹
Income taxes paid:	
Income tax expense for the year	7,000
<i>Add:</i> Income tax liability at the beginning of the year	<u>5,000</u>
	12,000
<i>Less:</i> Income tax liability at the end of the year	<u>(3,000)</u>
	<u>9,000</u>

Illustration 7

The balance sheets of Sun Ltd. as at 31st March 20X1 and 20X0 were as:

Particulars	Notes	20X1 ₹	20X0 ₹
Equity and Liabilities			
1 Shareholder's funds			
(a) Share capital	1	60,000	50,000
(b) Reserve & surplus	2	5,000	4,000
2 Current liabilities			
(a) Trade Payables		4,000	2,500
(b) Other current liabilities	3	-	1,000
(c) Short term provision (provision for tax)		1,500	1,000
Total		70,500	58,500
Assets			
1 Non-current assets			
(a) Property, Plant & Equipment	4	39,500	29,000
2 Current assets			
(a) Current investments		2,000	1,000
(b) Inventories		17,000	14,000
(c) Trade receivables		8,000	6,000
(d) Cash & cash equivalents	5	4,000	8,500
		70,500	58,500

Notes to accounts

		20X1	20X0
		₹	₹
1	Share Capital		
	<i>Equity Shares of ₹10 each</i>	<u>60,000</u>	<u>50,000</u>
2	Reserve & surplus		
	<i>Profit and Loss Account</i>	<u>5,000</u>	<u>4,000</u>
3	Other current liabilities		
	<i>Dividend Payable</i>	<u>-</u>	<u>1,000</u>
4	Property, plant and equipment (at WDV)		
	<i>Building</i>	10,000	10,000
	<i>Fixtures</i>	17,000	11,000
	<i>Vehicles</i>	<u>12,500</u>	<u>8,000</u>
	<i>Total</i>	<u>39,500</u>	<u>29,000</u>
5	Cash and cash equivalents		
	<i>Cash and Bank</i>	<u>4,000</u>	<u>8,500</u>

The profit and loss statement for the year ended 31st March, 20X1 disclosed:

Particulars	₹
Profit before tax	4,500
<i>Tax expense: Current tax</i>	<u>(1,500)</u>
<i>Profit for the year</i>	3,000
<i>Declared dividend</i>	<u>(2,000)</u>
<i>Retained Profit</i>	1,000

Further information is available:

	Fixtures	Vehicles
	₹	₹
<i>Depreciation for the year</i>	1,000	2,500
<i>Disposals:</i>		
<i>Proceeds on disposal of vehicles</i>	—	1,700
<i>Written down value</i>	—	<u>(1,000)</u>
<i>Profit on disposal</i>		<u>700</u>

Prepare a Cash Flow Statement for the year ended 31st March, 20X1.

Solution

Sun Ltd.
Cash Flow Statement
for the year ended 31st March, 20X1

	₹	₹
Cash flows from operating activities		
Net Profit before taxation	4,500	
Adjustments for:		
Depreciation	3,500	
Profit on sale of vehicles (1,700 – 1,000)	(700)	
Operating profit before working capital changes	7,300	
Increase in Trade receivables	(2,000)	
Increase in inventories	(3,000)	
Increase in Trade payables	1,500	
Cash generated from operations	3,800	
Income taxes paid (W.N.1)	(1,000)	
<i>Net cash generated from operating activities</i>		2,800

Cash flows from investing activities		
Sale of vehicles	1,700	
Purchase of current investments	(1,000)	
Purchase of vehicles (W.N.3)	(8,000)	
Purchase of fixtures (W.N.3)	(7,000)	
<i>Net cash used in investing activities</i>		(14,300)
Cash flows from financing activities		
Issue of shares for cash	10,000	
Dividends paid (W.N.2)	(3,000)	
<i>Net cash generated from financing activities</i>		<u>7,000</u>
Net decrease in cash and cash equivalents		(4,500)
Cash and cash equivalents at beginning of period (See Note)		8,500
Cash and cash equivalents at end of period (See Note)		4,000
Note to the Cash Flow Statement		
<i>Cash and Cash Equivalents</i>		
	31.3.20X1	31.3.20X0
Bank and Cash	4,000	8,500
Cash and cash equivalents	4,000	8,500

Working Notes:

			₹
1.	Income taxes paid		
	Income tax expense for the year		1,500
	<i>Add:</i> Income tax liability at the beginning of the year		1,000
			2,500
	<i>Less:</i> Income tax liability at the end of the year		(1,500)
			1,000
2.	Dividend paid		
	Declared dividend for the year		2,000
	<i>Add:</i> Amount payable at the beginning of the year		1,000
			3,000
	<i>Less:</i> Amount payable at the end of the year		-
			3,000
3.	Property, plant and equipment acquisitions		
		<i>Fixtures</i>	<i>Vehicles</i>
		₹	₹
	W.D.V. at 31.3.20X1	17,000	12,500
	<i>Add back:</i>		
	Depreciation for the year	1,000	2,500
	Disposals	—	1,000
		18,000	16,000
	<i>Less:</i> W.D.V. at 31.12.20X0	(11,000	(8,000)
)	
	Acquisitions during 20X0-20X1	7,000	8,000

Note: Current investments may not be readily convertible to a known amount of cash and may not be subject to an insignificant risk of changes in value as per the requirements of AS 3 and hence those have been considered as investing activities.

Illustration 8

Ms. Jyoti of Star Oils Limited has collected the following information for the preparation of cash flow statement for the year ended 31st March, 20X1:

	(₹ in lakhs)
Net Profit	25,000
Dividend paid	8,535
Provision for Income tax	5,000
Income tax paid during the year	4,248
Loss on sale of assets (net)	40
Book value of the assets sold	185
Depreciation charged to the Statement of Profit and Loss	20,000
Profit on sale of Investments	100
Carrying amount of Investment sold	27,765
Interest income received on investments	2,506
Interest expenses of the year	10,000
Interest paid during the year	10,520
Increase in Working Capital (excluding Cash & Bank Balance)	56,081
Purchase of Fixed assets	14,560
Investment in joint venture	3,850
Expenditure on construction work in progress	34,740
Proceeds from calls in arrear	2
Receipt of grant for capital projects	12
Proceeds from long-term borrowings	25,980
Proceeds from short-term borrowings	20,575
Opening cash and bank balance	5,003
Closing cash and bank balance	6,988

Prepare the Cash Flow Statement for the year ended 31 March 20X1 in accordance with AS 3. (Make necessary assumptions)

Solution

Star Oils Limited
Cash Flow Statement
for the year ended 31st March, 20X1

		(₹ in lakhs)
Cash flows from operating activities		
Net profit before taxation (25,000 + 5,000)	30,000	
Adjustments for :		
Depreciation	20,000	
Loss on sale of assets (Net)	40	
Profit on sale of investments	(100)	
Interest income on investments	(2,506)	
Interest expenses	10,000	
Operating profit before working capital changes	57,434	
Changes in working capital (Excluding cash and bank balance)	(56,081)	
Cash generated from operations	1,353	
Income taxes paid	(4,248)	
Net cash used in operating activities		(2,895)
Cash flows from investing activities		
Sale of assets (W.N.1)	145	
Sale of investments (27,765 + 100)	27,865	
Receipt of grant for capital projects	12	
Interest income on investments	2,506	
Purchase of fixed assets	(14,560)	
Investment in joint venture	(3,850)	
Expenditure on construction work-in progress	(34,740)	
Net cash used in investing activities		(22,622)

Cash flows from financing activities		
Proceeds from calls in arrear	2	
Proceeds from long-term borrowings	25,980	
Proceed from short-term borrowings	20,575	
Interest paid	(10,520)	
Dividend (including dividend tax) paid	<u>(8,535)</u>	27,502
Net increase in cash and cash equivalents		1,985
Cash and cash equivalents at the beginning of the period		5,003
Cash and cash equivalents at the end of the period		<u>6,988</u>

Working note:

1. Book value of the assets sold	185
Less : Loss on sale of assets	<u>(40)</u>
Proceeds on sale	<u>145</u>

Illustration 9

From the following Summary Cash Account of X Ltd. prepare Cash Flow Statement for the year ended 31st March, 20X1 in accordance with AS 3 (Revised) using the direct method. The company does not have any cash equivalents.

Summary Cash Account for the year ended 31.3.20X1

	₹000		₹000
Balance on 1.4.20X0	50	Payment to Suppliers	2,000
Issue of Equity Shares	300	Purchase of Fixed Asset	200
Receipts from Customers	2,800	Overhead expense	200
Sale of Fixed Assets	100	Wages and Salaries	100

		<i>Taxation</i>	250
		<i>Dividend</i>	50
		<i>Repayment of Bank Loan</i>	300
		<i>Balance on 31.3.20X1</i>	150
	3,250		3,250

Solution**X Ltd.**

Cash Flow Statement for the year ended 31st March, 20X1
(Using direct method)

	₹ '000	₹ '000
Cash flows from operating activities		
Cash receipts from customers	2,800	
Cash payments to suppliers	(2,000)	
Cash paid to employees	(100)	
Cash payments for overheads	(200)	
Cash generated from operations	500	
Income tax paid	(250)	
<i>Net cash generated from operating activities</i>		250
Cash flows from investing activities		
Payments for purchase of fixed assets	(200)	
Proceeds from sale of fixed assets	100	
<i>Net cash used in investing activities</i>		(100)
Cash flows from financing activities		
Proceeds from issuance of equity shares	300	
Bank loan repaid	(300)	
Dividend paid	(50)	
<i>Net cash used in financing activities</i>		(50)
Net increase in cash		100
Cash at the beginning of the year		50
Cash at the end of the year		150

Illustration 10

Given below are the relevant extracts of the Balance Sheet and the Statement of Profit and Loss of ABC Ltd. along with additional information:

Extract of Balance sheet

		Particulars	Notes	31.3.20X1 <i>(₹ in lakhs)</i>	31.3.20X0 <i>(₹ in lakhs)</i>
1		Equity and Liabilities			
		Current liabilities			
	(a)	Trade Payables		250	230
	(b)	Short term Provisions	1	200	180
	(c)	Other current liabilities	2	70	50
1		Assets			
		Current assets			
	(a)	Inventories		200	180
	(b)	Trade Receivables		400	250
	(c)	Other current assets	3	195	180

Statement of Profit and Loss of ABC Ltd.
for the year ended 31st March, 20X1

	Particulars	Notes	₹ in lakhs
I	Revenue from operations		4,150
II	Other income	4	<u>100</u>
III	Total income (I + II)		<u>4,250</u>
	Expenses:		
	Purchases of Stock-in-Trade		2,400
	Change in inventories of finished goods		(20)
	Employee benefits expense		800
	Depreciation expense		100
	Finance cost	5	60
	Other expenses		<u>200</u>
IV	Total expenses		<u>3,540</u>

V	Profit before tax (III – IV)		710
VI	Tax expense:		
	Current tax		200
VII	Profit for the year from continuing operations		510

Appropriations

Balance of Profit and Loss account brought forward	50
Transfer to general reserve	200
Dividend paid	330

Notes to accounts:

		20X1 (₹ in lakhs)	20X0 (₹ in lakhs)
1	Short term Provisions:		
	Provision for Tax	<u>200</u>	<u>180</u>
2	Other current liabilities:		
	Outstanding wages	50	40
	Outstanding expenses	<u>20</u>	<u>10</u>
	Total	<u>70</u>	<u>50</u>
3	Other current assets:		
	Advance tax	<u>195</u>	<u>180</u>
4	Other income:		
	Interest and dividend	<u>100</u>	
5	Finance cost:		
	Interest	<u>60</u>	

Compute cash flow from operating activities using both direct and indirect method.

Solution**Cash Flows from Operating Activities**

	<i>₹ in lakhs</i>	<i>₹ in lakhs</i>
Using Direct Method		
Cash Receipts:		
Cash sales and collection from Trade receivables		
Sales + Opening Trade receivables – Closing Trade receivables (A)	4,150 + 250 – 400	<u>4,000</u>
Cash payments:		
Cash purchases & payment to Trade payables		
Purchases + Opening Trade payables – Closing Trade payables	2,400 + 230 – 250	2,380
Wages and salaries paid	800 + 40 – 50	790
Cash expenses	200 + 10 – 20	190
Taxes paid – Advance tax		195
(B)		3,555
Cash flow from operating activities (A – B)		445
Using Indirect Method		
Profit before tax		710
<i>Add:</i> Non-cash items : Depreciation		100
<i>Add:</i> Interest : Financing cash inflow		60
<i>Less:</i> Interest and Dividend : Investment cash outflow		(100)
<i>Less:</i> Tax paid		(195)
Working capital adjustments		

Trade receivables	250–400	(150)	
Inventories	180–200	(20)	
Trade payables	250–230	20	
Outstanding wages	50–40	10	
Outstanding expenses	20–10	10	(130)
Cash flow from operating activities			<u>445</u>

Illustration 11

Prepare Cash flow for Gamma Ltd., for the year ending 31.3.20X1 from the following information:

- (1) Sales for the year amounted to ₹ 135 crores out of which 60% was cash sales.
- (2) Purchases for the year amounted to ₹ 55 crores out of which credit purchase was 80%.
- (3) Administrative and selling expenses amounted to ₹ 18 crores and salary paid amounted to ₹ 22 crores.
- (4) The Company redeemed debentures of ₹ 20 crores at a premium of 10%. Debenture holders were issued equity shares of ₹ 15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was ₹ 1.5 crores.
- (5) Dividend paid during the year amounted to ₹ 11.7 crores.
- (6) Investment costing ₹ 12 crores were sold at a profit of ₹ 2.4 crores.
- (7) ₹ 8 crores was paid towards income tax during the year.
- (8) A new plant costing ₹ 21 crores was purchased in part exchange of an old plant. The book value of the old plant was ₹ 12 crores but the vendor took over the old plant at a value of ₹ 10 crores only. The balance was paid in cash to the vendor.

(9) The following balances are also provided:

	₹ in crores 1.4.20X0	₹ in crores 31.3.20X1
Debtors	45	50
Creditors	21	23
Bank	6	18.2

Solution

Gamma Ltd.

Cash Flow Statement for the year ended 31st March, 20X1 (Using direct method)

Particulars	₹ in crores	₹ in crores
Cash flows from operating activities		
Cash sales (60% of 135)	81	
Cash receipts from Debtors [45+ (135x40%) - 50]	49	
Cash purchases (20% of 55)	(11)	
Cash payments to suppliers [21+ (55x80%) - 23]	(42)	
Cash paid to employees	(22)	
Cash payments for overheads (Adm. and selling)	(18)	
Cash generated from operations	37	
Income tax paid	(8)	
Net cash generated from operating activities		29
Cash flows from investing activities		
Sale of investments (12+ 2.40)	14.4	
Payments for purchase of fixed assets (21 - 10)	(11)	
Net cash generated from investing activities		3.4

Cash flows from financing activities		
Redemption of debentures (22-15)	(7)	
Interest paid	(1.5)	
Dividend paid	<u>(11.7)</u>	
Net cash used in financing activities		(20.2)
Net increase in cash		12.2
Cash at beginning of the period		6.0
Cash at end of the period		18.2

Significant non-cash items:

- Debenture-holders received equity shares of ₹ 15 crores on redemption of the debentures.
- Plant having book value of ₹ 12 crores was given in exchange of an asset costing ₹ 21 crores. The said plant was transferred at a value of ₹ 10 crores only, and ₹ 11 crores was paid for the balance dues towards the plant.

Illustration 12

From the following information of Mr. Zen, prepare a Cash flow statement as per AS-3 for the year ended 31.3.20X1:

Ledger balances of Mr. Zen as of 20X0 and 20X1

	As on 1.4.20X0	As on 1.4.20X1
	₹	₹
Zen's Capital A/c	10,00,000	12,24,000
Trade payables	3,20,000	3,52,000
Mrs. Zen's loan	2,00,000	--
Loan from Bank	3,20,000	4,00,000
Land	6,00,000	8,80,000
Plant and Machinery (net block)	6,40,000	4,40,000
Inventories	2,80,000	2,00,000
Trade receivables	2,40,000	4,00,000
Cash	80,000	56,000

Additional information:

A machine costing ₹ 80,000 (accumulated depreciation there on ₹24,000) was sold for ₹ 40,000. The provision for depreciation on 1.4.20X0 was ₹ 2,00,000 and 31.3.20X1 was ₹ 3,20,000. The net profit for the year ended on 31.3.20X1 was ₹ 3,60,000.

Solution

**Cash Flow Statement of Mr. Zen as per AS 3
for the year ended 31.3.20X1**

		₹
(i) Cash flow from operating activities		
Net Profit (given)		3,60,000
Adjustments for		
Depreciation on Plant & Machinery (W.N.2)	1,44,000	
Loss on Sale of Machinery (W.N.1)	16,000	1,60,000
Operating Profit before working capital changes		5,20,000
Decrease in inventories	80,000	
Increase in trade receivables	(1,60,000)	
Increase in trade payables	32,000	(48,000)
Net cash generated from operating activities		4,72,000
(ii) Cash flow from investing activities		
Sale of Machinery (W.N.1)	40,000	
Purchase of Land (8,80,000 – 6,00,000)	(2,80,000)	
Net cash used in investing activities		(2,40,000)

(iii) Cash flow from financing activities		
Repayment of Mrs. Zen's Loan	(2,00,000)	
Drawings (W.N.3)	(1,36,000)	
Loan from Bank	80,000	
Net cash used in financing activities		(2,56,000)
Net decrease in cash		(24,000)
Opening balance as on 1.4.20X0		80,000
Cash balance as on 31.3.20X1		56,000

Working Notes:
1. Plant & Machinery A/c

	₹		₹
To Balance b/d	8,40,000	By Cash – Sales	40,000
(6,40,000 + 2,00,000)		By Provision for Depreciation A/c	24,000
		By Profit & Loss A/c – Loss on Sale (80,000 – 64,000)	16,000
		By Balance c/d (4,40,000+3,20,000)	7,60,000
	8,40,000		8,40,000

2. Provision for depreciation on Plant and Machinery A/c

	₹		₹
To Plant and Machinery A/c	24,000	By Balance b/d	2,00,000
To Balance c/d	3,20,000	By Profit & Loss A/c (Bal. fig.)	1,44,000
	<u>3,44,000</u>		<u>3,44,000</u>

3. To find out Mr. Zen's drawings:

	₹
Opening Capital	10,00,000
<i>Add:</i> Net Profit	<u>3,60,000</u>
	13,60,000
<i>Less:</i> Closing Capital	<u>(12,24,000)</u>
Drawings	<u>1,36,000</u>

Note: Students may note that in case there is an increase in the amount of debentures/ loans during the year and the interest is required to be computed, then in such a case, students may choose either to compute interest on the closing balance of the debentures or may compute interest on opening balance for full year (in case of no repayment) and proportionate interest on additions. Suitable note for assumption may be given in the solution for this.

SUMMARY

- Cash flow statement dealt under AS 3.
- Benefits include providing information relating to changes in cash and cash equivalents of an enterprise.
- Cash include:
 - (a) Cash in hand and (b) Demand deposits with banks
- Cash equivalents are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.
- Cash flow activities may be classified as inflow and outflow but as per AS-3 they are classified as Operating Activities, Investing activities, Financing activities.
- Operating activities are principal revenue generating activities.
- Investing Activities relate to acquisition and disposal of long-term assets and other investments.

- Financing Activities include the ones which result in changes in the size and composition of the owner's capital (including preference share capital) and borrowings of the enterprise.
- Methods to calculate cash flow from operating activities include:
 - (a) Direct Method
 - (b) Indirect Method
- In order to calculate cash flow from investing activities inflows and outflows related to acquisition and disposal of assets, other than those related to operating activities, are shown under this category.
- In order to calculate cash flow from financing activities inflows and outflows related to the amount of capital and borrowings of the enterprise are shown under this head.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *While preparing cash flow statement, conversion of debt to equity*
 - (a) *Should be shown as a financing activity.*
 - (b) *Should be shown as an investing activity.*
 - (c) *Should not be shown as it is a non-cash transaction*
 - (d) *Should not be shown as operating activity.*
2. *Which of the following would be considered a 'cash-flow item from an "investing" activity'?*
 - (a) *Cash outflow to the government for payment of taxes.*
 - (b) *Cash outflow to purchase bonds issued by another company.*
 - (c) *Cash outflow to shareholders as dividends*
 - (d) *Cash outflow to make payment to trade payables.*

3. *All of the following would be included in a company's operating activities except:*
- (a) *Income tax payments*
 - (b) *Collections from customers or Cash payments to suppliers*
 - (c) *Dividend payments*
 - (d) *Office and selling expenses.*
4. *Hari Uttam, a stock broking firm, received ₹ 1,50,000 as premium for forward contracts entered for purchase of equity shares. How will you classify this amount in the cash flow statement of the firm?*
- (a) *Operating Activities.*
 - (b) *Investing Activities.*
 - (c) *Financing Activities.*
 - (d) *Non-cash transaction*
5. *As per AS 3 on Cash Flow Statements, cash received by a manufacturing company from sale of shares of ABC Company Ltd. should be classified as*
- (a) *Operating activity.*
 - (b) *Financing activity.*
 - (c) *Investing activity.*
 - (d) *Non-cash transaction*

Theoretical Questions

6. *What is the significance of cash flow statement? Explain in brief.*
7. *Explain the difference between direct and indirect methods of reporting cash flows from operating activities with reference to AS 3.*

Scenario based Questions

8. Classify the following activities as (a) Operating activities, (b) Investing activities (c) Financing activities (d) Cash equivalents with reference to AS 3 (Revised).
- Brokerage paid on purchase of investments
 - Underwriting commission paid
 - Trading commission received
 - Proceeds from sale of investment
 - Purchase of goodwill
 - Redemption of preference shares
 - Rent received from property held as investment
 - Interest paid on long-term borrowings
 - Marketable securities (having risk of change in value)
 - Refund of income tax received
9. How will you disclose following items while preparing Cash Flow Statement of Gagan Ltd. as per AS-3 for the year ended 31st March, 20X2?
- 10% Debentures issued:

As on 01-04-20X1	₹ 1,10,000
As on 31-03-20X2	₹ 77,000
 - Debentures were redeemed at 5% premium at the end of the year. Premium was charged to the Profit & Loss Account for the year.
 - Unpaid Interest on Debentures:

As on 01-04-20X1	₹ 275
As on 31-03-20X2	₹ 1,175
 - Debtors of ₹ 36,000 were written off against the Provision for Doubtful Debts A/c during the year.
 - 10% Bonds (Investments):

As on 01-04-20X1	₹ 3,50,000
As on 31-03-20X2	₹ 3,50,000
 - Accrued Interest on Investments:

As on 31-03-20X2	₹ 10,500
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10. From the following Balance sheet of Grow More Ltd., prepare Cash Flow Statement for the year ended 31st March, 20X1 :

Particulars		Notes	31 st March, 20X1	31 st March, 20X0
	Equity and Liabilities			
1	Shareholders' funds			
A	Share capital		10,00,000	8,00,000
B	Reserves and Surplus	1	3,00,000	2,10,000
2	Non-current liabilities			
	Long term borrowings	2	2,00,000	-
3	Current liabilities			
A	Trade Payables		7,00,000	8,20,000
B	Other current liabilities	3	-	1,00,000
C	Short term provision (provision for tax)		1,00,000	70,000
	Total		23,00,000	20,00,000
	Assets			
1	Non-current assets			
A	Property, plant and Equipment	4	13,00,000	9,00,000
B	Non-Current Investments		1,00,000	-
2	Current assets			
A	Inventories		4,00,000	2,00,000
B	Trade receivables		5,00,000	7,00,000
C	Cash and Cash equivalents		-	2,00,000
	Total		23,00,000	20,00,000

Notes to accounts

No.	Particulars	31 st March, 20X1	31 st March, 20X0
1	Reserves and Surplus		
	General reserve	2,00,000	1,50,000

	<i>Profit and Loss account</i>	<u>1,00,000</u>	<u>60,000</u>
	Total	<u>3,00,000</u>	<u>2,10,000</u>
2	Long term borrowings		
	<i>Debentures (issued at end of year)</i>	<u>2,00,000</u>	--
3.	Other current liabilities		
	<i>Dividend payable</i>	<u>-</u>	<u>1,00,000</u>
4	Property, plant and equipment		
	<i>Plant and machinery</i>	<u>7,00,000</u>	<u>5,00,000</u>
	<i>Land and building</i>	<u>6,00,000</u>	<u>4,00,000</u>
	Net carrying value	<u>13,00,000</u>	<u>9,00,000</u>

- (i) Depreciation @ 25% was charged on the opening value of Plant and Machinery.
- (ii) At the year end, one old machine costing ₹ 50,000 (WDV ₹ 20,000) was sold for ₹ 35,000. Purchase was also made at the year end.
- (iii) ₹ 50,000 was paid towards Income tax during the year.
- (iv) Construction of the building got completed on 31.03.20X1 and hence no depreciation may be charged on the same.

Prepare Cash flow Statement.

11. From the following Balance Sheets and information, prepare Cash Flow Statement of Ryan Ltd. by Indirect method for the year ended 31st March, 20X1:

Particulars		Notes	31 st March 20X1 ₹	31 st March 20X0 ₹
1	Equity and Liabilities			
	Shareholders' funds			

A	Share capital	1	6,00,000	7,00,000
B	Reserves and Surplus	2	4,20,000	3,00,000
2	Non-current liabilities			
	Long term borrowings	3	2,00,000	-
3	Current liabilities			
A	Trade Payables		1,15,000	1,10,000
B	Other current liabilities	4	30,000	80,000
C	Short term provision (provision for tax)		95,000	60,000
	Total		14,60,000	12,50,000
	Assets			
1	Non-current assets			
A	Property, plant and Equipment	5	9,15,000	7,00,000
B	Non-Current Investments		50,000	80,000
2	Current assets			
A	Inventories		95,000	90,000
B	Trade receivables		2,50,000	2,25,000
C	Cash and Cash equivalents		50,000	90,000
D	Other Current assets		1,00,000	65,000
	Total		14,60,000	12,50,000

Notes to accounts

No.		31 st March, 20X1	31 st March, 20X0
1.	Share capital		
	Equity share capital	6,00,000	5,00,000
	10% Redeemable Preference share capital	---	<u>2,00,000</u>
	Total	<u>6,00,000</u>	<u>7,00,000</u>

2	Reserves and Surplus		
	Capital redemption reserve	1,00,000	-
	Capital reserve	70,000	-
	General reserve	1,50,000	2,50,000
	Profit and Loss account	<u>1,00,000</u>	<u>50,000</u>
	Total	<u>4,20,000</u>	<u>3,00,000</u>
3	Long term borrowings		
	9% Debentures	<u>2,00,000</u>	--
4.	Other current liabilities		
	Dividend payable	-	60,000
	Liabilities for expenses	<u>30,000</u>	<u>20,000</u>
	Total	<u>30,000</u>	<u>80,000</u>
5	Property, plant and equipment		
	Plant and machinery	7,65,000	5,00,000
	Land and building	<u>1,50,000</u>	<u>2,00,000</u>
	Net carrying value	<u>9,15,000</u>	<u>7,00,000</u>

Additional Information:

- (i) A piece of land has been sold out for ₹1,50,000 (Cost – ₹1,20,000) and the balance land was revalued. Capital Reserve consisted of profit on revaluation of land.
- (ii) On 1st April, 20X0 a plant was sold for ₹90,000 (Original Cost – ₹70,000 and W.D.V. – ₹ 50,000) and Debentures worth ₹1 lakh were issued at par as part consideration for plant of ₹4.5 lakhs acquired.
- (iii) Part of the investments (Cost – ₹50,000) was sold for ₹70,000.

- (iv) Pre-acquisition dividend received ₹5,000 was adjusted against cost of investment.
- (v) Interim dividend was declared and paid @ 15% during the current year.
- (vi) Income-tax liability for the current year was estimated at ₹1,35,000.
- (vii) Depreciation @ 15% has been charged on Plant and Machinery but no depreciation has been charged on Building.
12. The Balance Sheet of New Light Ltd. as at 31st March, 20X1 and 20X0 (for the years ended) are as follows:

		Notes	₹ 31 st March 20X0	₹ 31 st March 20X1	
	Equity and Liabilities				
1	Shareholders' funds				
	A	Share capital	1	16,00,000	18,80,000
	B	Reserves and Surplus	2	8,40,000	11,00,000
2	Non-current liabilities				
		Long term borrowings	3	4,00,000	2,80,000
3	Current liabilities				
	A	Other current liabilities	4	6,00,000	5,20,000
	B	Short term provision (provision for tax)		3,60,000	3,40,000
		Total		38,00,000	41,20,000
	Assets				
1	Non-current assets				
	A	Property, plant and Equipment	5	22,80,000	26,40,000
	B	Non-Current Investments		4,00,000	3,20,000
2	Current assets				
	A	Cash and Cash equivalents		10,000	10,000

	B	Other Current assets		11,10,000	11,50,000
		Total		38,00,000	41,20,000

Notes to accounts

No.	Particulars	31 st March, 20X0	31 st March, 20X1
1.	Share capital		
	Equity share capital	12,00,000	16,00,000
	10% Preference share capital	<u>4,00,000</u>	<u>2,80,000</u>
	Total	<u>16,00,000</u>	<u>18,80,000</u>
2	Reserves and Surplus		
	General reserve	6,00,000	7,60,000
	Profit and Loss account	<u>2,40,000</u>	<u>3,40,000</u>
	Total	<u>8,40,000</u>	<u>11,00,000</u>
3	Long term borrowings		
	9% Debentures	<u>4,00,000</u>	<u>2,80,000</u>
	Total	<u>4,00,000</u>	<u>2,80,000</u>
4.	Other current liabilities		
	Dividend payable	1,20,000	-
	Current Liabilities	<u>4,80,000</u>	<u>5,20,000</u>
	Total	<u>6,00,000</u>	<u>5,20,000</u>
5	Property, plant and equipment		
	Property, plant and equipment	32,00,000	38,00,000
	Less: Depreciation	<u>(9,20,000)</u>	<u>(11,60,000)</u>
	Net carrying value	<u>22,80,000</u>	<u>26,40,000</u>

Additional information:

- (i) The company sold one property, plant and equipment for ₹ 1,00,000, the

cost of which was ₹ 2,00,000 and the depreciation provided on it was ₹80,000.

- (ii) The company also decided to write off another item of property, plant and equipment costing ₹ 56,000 on which depreciation amounting to ₹ 40,000 has been provided.
- (iii) Depreciation on property, plant and equipment provided ₹ 3,60,000.
- (iv) Company sold some investment at a profit of ₹ 40,000.
- (v) Debentures and preference share capital redeemed at 5% premium. Debentures were redeemed at the year end.
- (vi) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31.3.20X0 was ₹ 2,16,000. The inventory on 31.3.20X1 was correctly valued at ₹ 3,00,000.

Prepare Cash Flow Statement as per revised Accounting Standard 3 by indirect method.

13. ABC Ltd. gives you the Balance sheets as at 31st March 20X0 and 31st March 20X1. You are required to prepare Cash Flow Statement by using indirect method as per AS 3 for the year ended 31st March 20X1:

Particulars		Notes	₹	₹
			31 st March 20X0	31 st March 20X1
1	Equity and Liabilities			
	Shareholders' funds			
	A Share capital		50,00,000	50,00,000
	B Reserves and Surplus		26,50,000	36,90,000
2	Non-current liabilities			
	Long term borrowings	1	-	9,00,000

3	Current liabilities			
A	Short-term borrowings (Bank loan)		1,50,000	3,00,000
B	Trade payables		8,80,000	8,20,000
C	Other current liabilities	2	4,80,000	2,70,000
	Total		91,60,000	1,09,80,000
	Assets			
1	Non-current assets			
A	Property, plant and Equipment	3	21,20,000	32,80,000
2	Current assets			
A	Current Investments		11,80,000	15,00,000
B	Inventory		20,10,000	19,20,000
C	Trade receivables	4	22,40,000	26,40,000
D	Cash and Cash equivalents		15,20,000	15,20,000
E	Other Current assets (Prepaid expenses)		90,000	1,20,000
	Total		91,60,000	1,09,80,000

Notes to accounts

No.	Particulars		₹20X0	20X1
1	Long term borrowings			
	9% Debentures (issued at the end of year)		-	<u>9,00,000</u>
	Total		-	<u>9,00,000</u>
2.	Other current liabilities			
	Dividend payable		1,50,000	-
	Liabilities for expenses		<u>3,30,000</u>	<u>2,70,000</u>
	Total		<u>4,80,000</u>	<u>2,70,000</u>

3	Property, plant and equipment		
	Plant and machinery	27,30,000	40,70,000
	Less: Depreciation	(6,10,000)	(7,90,000)
	Net carrying value	21,20,000	32,80,000
4	Trade receivables		
	Gross amount	23,90,000	28,30,000
	Less: Provision for doubtful debts	(1,50,000)	(1,90,000)
	Total	22,40,000	26,40,000

Additional Information:

- (i) Net profit for the year ended 31st March, 20X1, after charging depreciation ₹ 1,80,000 is ₹ 10,40,000.
- (ii) Trade receivables of ₹ 2,30,000 were determined to be worthless and were written off against the provisions for doubtful debts account during the year.
14. Following is the Balance Sheet of Fox Ltd. You are required to prepare cash flow statement using Indirect Method.

Particulars	Note No.	31 st March, 20X2 (₹)	31 st March, 20X1 (₹)
(I) Equity and Liabilities			
1. Shareholders' Funds			
(a) Share capital	1	5,60,000	3,00,000
(b) Reserve and Surplus	2	35,000	25,000
2. Current Liabilities			
(a) Trade payables		1,50,000	60,000
(b) Short-term provisions (Provision for taxation)		8,000	5,000
Total		7,53,000	3,90,000

(II) Assets			
1. Non-current assets			
(a) Property, Plant and Equipment		3,50,000	1,80,000
2. Current assets			
(a) Inventories		1,20,000	50,000
(b) Trade receivables		1,00,000	25,000
(c) Cash and cash equivalents		1,05,000	90,000
(d) Other current assets		78,000	45,000
Total		7,53,000	3,90,000

Notes to Accounts

Particulars	31 st	31 st
	March, 20X2 (₹)	March, 20X1 (₹)
1. Share capital		
(a) Equity share capital	4,10,000	2,00,000
(b) Preference share capital	<u>1,50,000</u>	<u>1,00,000</u>
	<u>5,60,000</u>	<u>3,00,000</u>
2. Reserve and surplus		
Surplus in statement of profit and loss at the beginning of the year	25,000	
Add: Profit of the year	20,000	
Less: Dividend	<u>(10,000)</u>	
Surplus in statement of profit and loss at the end of the year	35,000	25,000

Additional Information:

1. Dividend paid during the year ₹ 10,000
2. Depreciation charges during the year ₹ 40,000.

ANSWERS/ HINTS

Answer to the Multiple Choice Questions

1.	(c)	2.	(b)	3.	(c)	4.	(a)	5.	(c)		
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Answer to the Theoretical Questions

6. Cash flow statement provides information about the changes in cash and cash equivalents of an enterprise. It identifies cash generated from trading operations and is very useful tool of planning.
7. As per Para 18 of AS 3 (Revised) on Cash Flow Statements, an enterprise should report cash flows from operating activities using either:
- The direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed; or
 - the indirect method, whereby net profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows.

Answer to the Scenario based Questions

8. **Classification of activities with reference to AS 3**

a.	Brokerage paid on purchased of investments	Investing Activities
b.	Underwriting Commission paid	Financing Activities
c.	Trading Commission received	Operating Activities
d.	Proceeds from sale of investment	Investing Activities
e.	Purchase of goodwill	Investing Activities
f.	Redemption of Preference shares	Financing Activities
g.	Rent received from property held as investment	Investing Activities

h.	Interest paid on long term borrowings	Financing Activities
i.	Marketable securities	Not a Cash equivalent
j.	Refund of Income tax received	Operating activities

9.

**Cash Flow Statement of M/s Gagan Ltd.
for the year ended March 31, 20X2**

A	Cash Flow from Operating Activities	
	Net Profit as per Profit & Loss A/c	xxxxx
	Add: Premium on Redemption of Debentures	1,650
	Add: Interest on 10% Debentures	11,000
	Less: Interest on 10% Investments	(35,000)
B	Cash Flow from Investing Activities	
	Interest on Investments [35,000-10,500]	24,500
C	Cash Flow from Financing Activities	
	Interest on Debentures paid [11,000 - (1,175 - 275)] - outflow	(10,100)
	Redemption of Debentures [(1,10,000 - 77,000) at 5% premium] - outflow	(34,650)

Note: Debtors written off against provision for doubtful debts does not require any further adjustment in Cash Flow Statement.

10.

**Cash Flow Statement of Grow More Ltd.
for the year ended 31st March, 20X1
Cash Flow from Operating Activities**

		₹
Increase in balance of Profit and Loss Account (1,00,000 – 60,000)	40,000	
Provision for taxation (W.N.1)	80,000	
Transfer to General Reserve (2,00,000 – 1,50,000)	50,000	
Depreciation (W.N.2)	1,25,000	

Profit on sale of Plant and Machinery	(15,000)	
Operating Profit before Working Capital changes	2,80,000	
Increase in Inventories	(2,00,000)	
Decrease in Trade receivables	2,00,000	
Decrease in Trade payables	(1,20,000)	
Cash generated from operations	1,60,000	
Income tax paid	(50,000)	
Net Cash generated from operating activities		1,10,000

Cash Flow from Investing Activities

Purchase of fixed assets	(3,45,000)	
Expenses on building (6,00,000 – 4,00,000)	(2,00,000)	
Increase in investments	(1,00,000)	
Sale of old machine	35,000	
Net Cash used in investing activities		(6,10,000)

Cash Flow from Financing activities

Proceeds from issue of shares (10,00,000 – 8,00,000)	2,00,000	
Proceeds from issue of debentures	2,00,000	
Dividend paid	<u>(1,00,000)</u>	
Net cash generated from financing activities		<u>3,00,000</u>
Net decrease in cash and cash equivalents		(2,00,000)
Cash and Cash equivalents at the beginning of the year		<u>2,00,000</u>
Cash and Cash equivalents at the end of the year		<u>Nil</u>

Working Notes:**1. Provision for taxation account**

	₹		₹
To Cash (Paid)	50,000	By Balance b/d	70,000
To Balance c/d	1,00,000	By Profit and Loss A/c	80,000
	_____	(Balancing figure)	_____
	<u>1,50,000</u>		<u>1,50,000</u>

2. Plant and Machinery account

	₹		₹
To Balance b/d	5,00,000	By Depreciation	1,25,000
To Profit and Loss A/c (profit on sale of machine)	15,000		
To Cash (Balancing figure)	3,45,000	By Cash (sale of machine)	35,000
	_____	By Balance c/d	<u>7,00,000</u>
	<u>8,60,000</u>		<u>8,60,000</u>

11.

**Cash Flow Statement of Ryan Limited
For the year ended 31st March, 20X1**

	₹	₹
Cash flow from operating activities		
Net Profit before taxation (W.N.1)	2,75,000	
Adjustment for		
Depreciation (W.N.3)	1,35,000	
Profit on sale of land	(30,000)	

Profit on sale of plant (W.N.3)	(40,000)	
Profit on sale of investments (W.N.4)	(20,000)	
Interest on debentures (2,00,000 X 9%)	18,000	
Operating profit before working capital changes	3,38,000	
Increase in inventory	(5,000)	
Increase in trade receivables	(25,000)	
Increase in Other current assets (W.N.9)	(35,000)	
Increase in Trade payables	5,000	
Increase in liabilities for expenses	10,000	
Cash generated from operations	2,88,000	
Income taxes paid (W.N.8)	(1,00,000)	
Net cash generated from operating activities		1,88,000
Cash flow from investing activities		
Proceeds from sale of land (W.N.2)	1,50,000	
Proceeds from sale of plant (W.N.3)	90,000	
Proceeds from sale of investments (W.N.4)	70,000	
Purchase of plant (W.N.3)	(3,50,000)	
Purchase of investments (W.N.4)	(25,000)	
Pre-acquisition dividend received (W.N.4)	5,000	
Net cash used in investing activities		(60,000)
Cash flow from financing activities		
Proceeds from issue of equity shares (6,00,000 – 5,00,000)	1,00,000	
Proceeds from issue of debentures (2,00,000 – 1,00,000)	1,00,000	
Redemption of preference shares	(2,00,000)	
Dividends paid	(1,50,000)	

Interest paid on debentures	(18,000)	
Net cash used in financing activities		(1,68,000)
Net decrease in cash and cash equivalents		(40,000)
Cash and cash equivalents at the beginning of the year		90,000
Cash and Cash equivalents at the end of the year		50,000

Significant Non-cash Items:

Debentures amounting to ₹ 1,00,000 have been issued as part consideration for acquisition of plant of ₹ 4,50,000.

Working Notes:

1.		₹
	Net profit before taxation	
	Retained profit	1,00,000
	Less: Balance as on 31.3.20X0	(50,000)
		50,000
	Provision for taxation	1,35,000
	Dividend	90,000
		2,75,000

2. **Land and Building Account**

	₹		₹
To Balance b/d	2,00,000	By Cash (Sale)	1,50,000
To Profit and Loss A/c (Profit on sale)	30,000	By Balance c/d	1,50,000
To Capital reserve (Revaluation profit)	70,000		
	3,00,000		3,00,000

3. **Plant and Machinery Account**

	₹		₹
To Balance b/d	5,00,000	By Cash (Sale)	90,000
To Profit and loss account	40,000	By Depreciation	1,35,000
To Debentures	1,00,000	By Balance c/d	7,65,000
To Bank	3,50,000		
	<u>9,90,000</u>		<u>9,90,000</u>

4. **Investments Account**

	₹		₹
To Balance b/d	80,000	By Cash (Sale)	70,000
To Profit and loss account	20,000	By Dividend (Pre-acquisition)	5,000
To Bank (Balancing figure)	25,000	By Balance c/d	50,000
	<u>1,25,000</u>		<u>1,25,000</u>

5. **Capital Reserve Account**

	₹		₹
To Balance c/d	70,000	By Profit on revaluation of land	70,000
	<u>70,000</u>		<u>70,000</u>

6. **General Reserve Account**

	₹		₹
To Capital redemption reserve	1,00,000	By Balance b/d	2,50,000
To Balance c/d	1,50,000		
	<u>2,50,000</u>		<u>2,50,000</u>

7. **Dividend payable Account**

	₹		₹
To Bank (Balancing figure)	1,50,000	By Balance b/d	60,000
To Balance c/d	-	By Profit and loss account	90,000
	1,50,000		1,50,000

8. **Provision for Taxation Account**

	₹		₹
To Bank (Balancing figure)	1,00,000	By Balance b/d	60,000
To Balance c/d	95,000	By Profit and loss account	1,35,000
	1,95,000		1,95,000

9. **Other Current Assets Account**

	₹		₹
To Balance b/d	65,000	By Balance c/d	1,00,000
To Bank (Balancing figure)	35,000		
	1,00,000		1,00,000

12. **New Light Ltd.****Cash Flow Statement for the year ended 31st March, 20X1**

A.	Cash Flow from operating activities	₹	₹
	Profit after appropriation		
	Increase in profit and loss A/c after inventory adjustment [₹3,40,000 – (₹2,40,000 + ₹24,000)]	76,000	

Transfer to general reserve	1,60,000	
Provision for tax	3,40,000	
Net profit before taxation and extraordinary item	5,76,000	
Adjustments for:		
Depreciation	3,60,000	
Loss on sale of property, plant and equipment	20,000	
Decrease in value of property, plant and equipment	16,000	
Profit on sale of investment	(40,000)	
Premium on redemption of preference share capital	6,000	
Interest on debentures	36,000	
Premium on redemption of debentures	6,000	
Operating profit before working capital changes	9,80,000	
Increase in current liabilities (₹5,20,000 – ₹4,80,000)	40,000	
Increase in other current assets [₹11,50,000 – (₹ 11,10,000 + ₹24,000)]	(16,000)	
Cash generated from operations	10,04,000	
Income taxes paid	(3,60,000)	
Net Cash generated from operating activities		6,44,000
B. Cash Flow from investing activities		
Purchase of property, plant and equipment (W.N.3)	(8,56,000)	
Proceeds from sale of property, plant and equipment (W.N.3)	1,00,000	

	Proceeds from sale of investments (W.N.2)	1,20,000	
	Net Cash used in investing activities		(6,36,000)
C.	Cash Flow from financing activities		
	Proceeds from issuance of share capital	4,00,000	
	Redemption of preference share capital (₹1,20,000 + ₹6,000)	(1,26,000)	
	Redemption of debentures (₹ 1,20,000 + ₹ 6,000)	(1,26,000)	
	Dividend paid	(1,20,000)	
	Interest on debentures	(36,000)	
	Net Cash generated from financing activities		(8,000)
	Net increase/decrease in cash and cash equivalent during the year		Nil
	Cash and cash equivalent at the beginning of the year		10,000
	Cash and cash equivalent at the end of the year		10,000

Working Notes:

1. Revaluation of inventory will increase opening inventory by ₹ 24,000.

$$2,16,000/90 \times 10 = ₹ 24,000$$

Therefore, opening balance of other current assets would be as follows:

$$₹ 11,10,000 + ₹ 24,000 = ₹ 11,34,000$$

Due to under valuation of inventory, the opening balance of profit and loss account be increased by ₹ 24,000.

The opening balance of profit and loss account after revaluation of inventory will be ₹ 2,40,000 + ₹ 24,000 = ₹ 2,64,000

2.

Investment Account

	₹		₹
To Balance b/d	4,00,000	By Bank A/c	1,20,000
To Profit and Loss A/c (Profit on sale of investment)	40,000	By (balancing figure being investment sold)	
		By Balance c/d	3,20,000
	<u>4,40,000</u>		<u>4,40,000</u>

3.

Property, Plant and Equipment Account

	₹		₹	₹
To Balance b/d	32,00,000	By Bank A/c (sale of assets)	1,00,000	
To Bank A/c (balancing figure being assets purchased)	8,56,000	By Accumulated depreciation A/c	80,000	
		By Profit and loss A/c (loss on sale of assets)	20,000	2,00,000
		By Accumulated depreciation A/c	40,000	
		By Profit and loss A/c (assets written off)	<u>16,000</u>	56,000
		By Balance c/d		<u>38,00,000</u>
	<u>40,56,000</u>			<u>40,56,000</u>

4. **Accumulated Depreciation Account**

	₹		₹
To Property, plant and equipment A/c	80,000	By Balance b/d	9,20,000
To Property, plant and equipment A/c	40,000	By Profit and loss A/c (depreciation for the year)	3,60,000
To Balance c/d	11,60,000		
	12,80,000		12,80,000

13. **Cash Flow Statement of ABC Ltd. for the year ended 31.3.20X1**

Cash flows from Operating Activities	₹	₹
Net Profit	10,40,000	
<i>Add:</i> Adjustment For Depreciation (₹7,90,000 – ₹6,10,000)	1,80,000	
<i>Add:</i> Adjustment for Provision for Doubtful Debts (₹ 4,20,000 – ₹1,50,000)	2,70,000	
Operating Profit Before Working Capital Changes	14,90,000	
<i>Add:</i> Decrease in Inventories (₹ 20,10,000 – ₹ 19,20,000)	90,000	
	15,80,000	
<i>Less:</i> Increase in Current Assets		
Trade Receivables (₹ 30,60,000 – ₹23,90,000)	6,70,000	
Prepaid Expenses (₹ 1,20,000 – ₹90,000)	30,000	

Decrease in Current Liabilities:		
Trade Payables (₹ 8,80,000 – ₹ 8,20,000)	60,000	
Expenses Outstanding (₹ 3,30,000 – ₹ 2,70,000)	<u>60,000</u>	(8,20,000)
<i>Net Cash generated from Operating Activities</i>		7,60,000
Cash Flows from Investing Activities		
Investment in Current Investments		(3,20,000)
Purchase of Plant & Machinery (₹ 40,70,000 – ₹ 27,30,000)		<u>(13,40,000)</u>
<i>Net Cash Used in Investing Activities</i>		(16,60,000)
Cash Flows from Financing Activities		
Bank Loan Raised (₹ 3,00,000 – ₹ 1,50,000)		1,50,000
Issue of Debentures		9,00,000
Payment of Dividend		<u>(1,50,000)</u>
Net Cash Used in Financing Activities		9,00,000
Net Increase in Cash During the Year		-
<i>Add: Cash and Cash Equivalents as on 1.4.20X0</i>		15,20,000
Cash and Cash Equivalents as on 31.3.20X1		15,20,000

Note:

- Bad debts amounting ₹ 2,30,000 were written off against provision for doubtful debts account during the year. In the above solution, Bad debts have been added back in the balances of provision for doubtful debts and trade receivables as on 31.3.20X1. Alternatively, the adjustment of writing off bad debts may be ignored and the solution can be given on the basis of figures of trade receivables and provision for doubtful debts as appearing in the balance sheet on 31.3.20X1.

2. Current investments (i.e. Marketable securities) may not be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value as per the requirements of AS 3 and hence those have been considered as investing activities.

14.

Fox Ltd.**Cash Flow Statement for the year ended 31st March, 20X2**

	₹	₹
<u>Cash flows from operating activities</u>		
Net Profit (35,000 less 25,000)	10,000	
Add: Dividend	10,000	
Provision for tax	<u>8,000</u>	
Net profit before taxation and extraordinary items	28,000	
Adjustments for:		
Depreciation	40,000	
Operating profit before working capital changes		68,000
Increase in trade receivables	(75,000)	
Increase in inventories	(70,000)	
Increase in other current assets	(33,000)	
Increase in trade payables	90,000	(88,000)
<i>Cash used in operating activities</i>		(20,000)
Less: Tax paid*		(5,000)
<i>Net cash used in operating activities</i>		(25,000)
<u>Cash flows from investing activities</u>		
Purchase of PPE	(2,10,000)	
<i>Net cash used in investing activities</i>		(2,10,000)

<u>Cash flows from financing activities</u>		
Issue of equity shares for cash	2,10,000	
Issue of preference shares	50,000	
Dividends paid	(10,000)	
<i>Net cash generated from financing activities</i>		2,50,000
Net increase in cash and cash equivalents		15,000
Cash and cash equivalents at beginning of period		90,000
Cash and cash equivalents at end of period		1,05,000

*Provision for tax of last year considered to be paid in the current year.

Working Note:

	₹
Property, plant and equipment acquisitions	
W.D.V. at 31.3.20X2	3,50,000
<i>Add back:</i>	
Depreciation for the year	40,000
	3,90,000
<i>Less: W.D.V. at 31.12.20X1</i>	1,80,000
Acquisitions during 20X1-20X2	2,10,000