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Cash Flow From Investing Activities → Direct Method / Indirect Method : Same Format

1. Purchase of Land / Building / Investments (Shares / Deb)	C. Outflow	
2. Sale of Land / Building / Investments	C. Inflow	
3. Interest Received	C. "	
4. Dividend Received	C. "	
5. Acquisition of a Subsidiary Company	C. Outflow	
6. Sale of a Subsidiary Company	C. Inflow	
7. Loan / Advances given	C. Outflow	
8. Loan / Advances recovered	C. Inflow	

NOTE :- If the above transactions are for consideration other than cash, then the same will not be covered in cash flow statement.

Cash Flow From Financing Activities → Direct / Indirect Method : Same Format

Particulars	Amount	Amount
1) Issue of Share Capital	C.I	
2) Buyback / Redemption of Share Capital	C.O	
3) Bank Loan Raised	C.I.	
4) Bank Loan Repaid	C.O	
5) Debentures issued	C.I	
6) Debentures redeemed	C.O	
7) Interest paid	C.O	
8) Dividend paid	C.O	

NOTE :- If the above activities are done for non-cash consideration, the same will not be covered in the cash flow statement.

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LOANS & ADVANCES GIVEN

- By Financial Entity → Operating Activity
- By Non-Financial Entity → Investing Activity
- To Subsidiary Companies → Investing Activity
- To, Employees → Operating Activity
- To, Suppliers → Operating Activity

* Interest on the above will be treated under the same classification as is used for Loans & Advances given.

* Interest earned from customers for late payment is treated under operating cash flow for a non-financial entity.

LOANS AND ADVANCES TAKEN

- By, Financial Entity → Operating Activity
- By, Non financial Entity → Financing Activity
- From Subsidiary company → Financing activity
- From Customer → Operating Activity

* Interest paid to suppliers for late payment → Operating Activity.
* Interest included in Inventory as per AS-16 → Operating Activity.

INVESTMENT MADE AND DIVIDEND EARNED

- For Financial Entity in normal course of business → Operating Activity
- For Non-financial Entity → Investing Activity
- Investment in subsidiary for all enterprises → Investing Activity

DIVIDEND PAID

→ It is always treated as a financing activity for any type of entity.

* Dividend is paid on Share Capital Issued which can never be considered as an operating activity for any business.

* Share Capital Issued is always a financing activity for any kind of business.

TREATMENT OF TAX/TDS

→ Tax paid on operating income → operating cash flow.

TDS

- **Against Income**
  - Eg: Interest Income
    - Financing Entity ↓ Operating Inc. ↓ TDS = OA.
    - Non-financing Entity ↓ Investing Inc ↓ TDS = IA
- **Against Expenses**
  - Eg: Interest Expense
    - Financing Entity ↓ Operating Exp ↓ TDS = OA.
    - Non-financing Entity ↓ Financing Exp ↓ TDS = FA

INSURANCE CLAIM

- 1. Loss of Stock
  2. Loss of Profit
  ↓
  Operating Activity)
  (Extraordinary)
- 1. Loss of Fixed Asset
  (Plant & Mach/Build.)
  ↓
  Investing Activity
  (Extraordinary)

BUSINESS PURCHASE

1. Acquisition of a business } Investing Activities
   Disposal " " "

2. Both should be presented separately & not netted off.

3. Disclose :- Amount of purchase consideration
   Portion of purchase consideration received as cash and cash equivalents.

Treatment of current Assets & Liabilities takenover during Business Purchase

1.1 — 31.3

Bus. Purchase

CA Takenover (TO)

CL TO

CA (self) + CA (TO) = Total CA

CL (self) + CL (TO) = Total CL

Calculation of Increase/Decrease in C.A and Increase/Decrease in C.L.
(Δ in working capital)

→ Closing bal of current Assets = Total C.A. − C.A Takenover
= C.A. (self) → closing bal.

− Opening bal of current Assets

Changes in current Assets

→ Closing bal of current Liab = Total C.L. − C.L. Takenover
= C.L. (self) → closing bal.

− Opening bal of current Liab

Changes in current Liab

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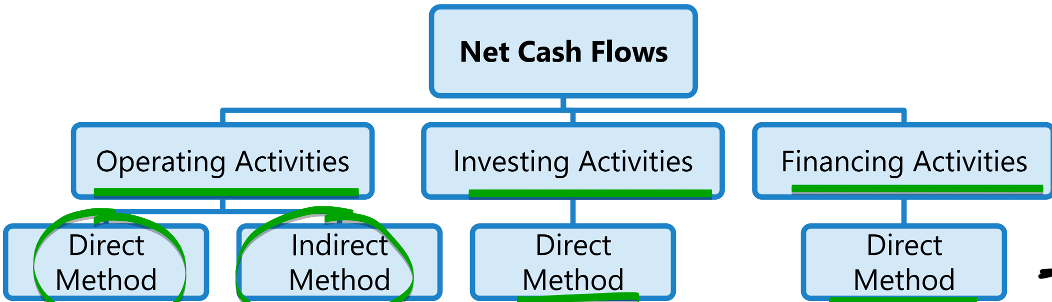
and borrowings of the enterprise. Examples include issue of shares / debentures, redemption of debentures / preference shares, payment of dividends and payment of interests (other than interests paid by financial institutions).

2.6 IDENTIFYING TYPE OF CASH FLOWS

Classification of Cash Flows



FE
→ Borrowing
→ Lending
→ Investments

Cash flow type depends on the business of the enterprise and other factors. For example, since principal business of financial enterprises consists of borrowing, lending and investing, loans given and interests earned are operating cash flows for financial enterprises and investing cash flows for other enterprises. A few typical cases are discussed below.

2.6.1 Loans/Advances given and Interests earned

(a) Loans and advances given and interests earned on them in the ordinary course of business are operating cash flows for financial enterprises.

(b) Loans and advances given and interests earned on them are investing cash flows for non-financial enterprises.

(c) Loans and advances given to subsidiaries and interests earned on them are investing cash flows for all enterprises.

(d) Loans and advances given to employees and interests earned on them are operating cash flows for all enterprises.

(e) Advance payments to suppliers and interests earned on them are operating cash flows for all enterprises.

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(f) Interests earned from customers for late payments are operating cash flows for non-financial enterprises.

2.6.2 Loans/Advances taken and interests paid

Type of Co.

(a) Loans and advances taken and interests paid on them in the ordinary course of business are operating cash flows for financial enterprises.

(b) Loans and advances taken and interests paid on them are financing cash flows for non-financial enterprises.

(c) Loans and advances taken from subsidiaries and interests paid on them are financing cash flows for all enterprises.

(d) Advance taken from customers and interests paid on them are operating cash flows for non-financial enterprises.

(e) Interests paid to suppliers for late payments are operating cash flows for all enterprises.

(f) Interests taken as part of inventory costs in accordance with AS 16 are operating cash flows.

2.6.3 Investments made and dividends earned

(a) Investments made and dividends earned on them in the ordinary course of business are operating cash flows for financial enterprises.

(b) Investments made and dividends earned on them are investing cash flows for non-financial enterprises.

(c) Investments in subsidiaries and dividends earned on them are investing cash flows for all enterprises.

Invest → Interest Inc. → TDS → Invest A

2.6.4 Dividends Paid

Dividends paid are $\boxed{\text{financing cash outflows}}$ for all enterprises.

2.6.5 Income Tax

(a) Tax paid on operating income is operating cash outflows for all enterprises

(b) Tax deducted at source against income are operating cash outflows if concerned incomes are operating incomes and investing cash outflows if the concerned incomes are investment incomes, e.g. interest earned.

(c) Tax deducted at source against expenses are operating cash inflows if concerned expenses are operating expenses and financing cash inflows if the concerned expenses are financing expenses, e.g. interests paid.

2.6.6 Insurance claims received

(a) Insurance claims received against loss of stock or loss of profits are extraordinary operating cash inflows for all enterprises.

(b) Insurance claims received against loss of fixed assets are extraordinary investing cash inflows for all enterprises.

AS 3 requires separate disclosure of extraordinary cash flows, classifying them as cash flows from operating, investing or financing activities, as may be appropriate.

2.7 REPORTING CASH FLOWS FROM OPERATING ACTIVITIES

Net cash flow from operating activities can be reported either as direct method or as indirect method.

In **'Direct method'** we take the gross receipts from sales, trade receivables and other operating inflows subtracted by gross payments for purchases, creditors and other expenses ignoring all non-cash items like depreciation, provisions.

In '**Indirect method**' we start from the net profit or loss figure, eliminate the effect of any non-cash items, investing items and financing items from such profit figure i.e. all such expenses like depreciation, provisions, interest paid, loss on sale of assets etc. are added and interest received etc. are deducted. Adjustment for changes in working capital items are also made ignoring cash and cash equivalent to reach to the figure of net cash flow.

Direct method is preferred over indirect because, direct method gives us the clear picture of various sources of cash inflows and outflows which helps in estimating the future cash inflows and outflows.

Bus sold C·I x
- Bus purch L·O x
Net fig. x

1·1· BP CA CL

31·3 CA CL CA CL

L55

of a

2.9 BUSINESS PURCHASE

The aggregate cash flows arising from acquisitions and disposals of subsidiaries or other business units should be presented separately and classified as cash flow from investing activities.

(a) The cash flows from disposal and acquisition should not be netted off.

(b) An enterprise should disclose, in aggregate, in respect of both acquisition and disposal of subsidiaries or other business units during the period each of the following:

(i) The total purchase or disposal consideration; and

(ii) The portion of the purchase or disposal consideration discharged by means of cash and cash equivalents.

Treatment of current assets and liabilities taken over on business purchase

Business purchase is not operating activity. Thus, while taking the differences between closing and opening current assets and liabilities for computation of operating cash flows, the closing balances should be reduced by the values of current assets and liabilities taken over. This ensures that the differences reflect the increases/decreases in current assets and liabilities due to operating activities only.

2.10 EXCHANGE GAINS AND LOSSES

Inc/Dec.
Debtors → ΔWC

10000 $
× ER
[Closing Date]

The foreign currency monetary assets (e.g. balance with bank, debtors etc.) and liabilities (e.g. creditors) are initially recognised by translating them into reporting currency by the rate of exchange transaction date. On the balance sheet date, these are restated using the rate of exchange on the balance sheet date. The difference in values is exchange gain/loss. The exchange gains and losses are recognised in the statement of profit and loss.

US → Central Bank : 5000 $ × ER
[closing date]

The exchange gains/losses in respect of cash and cash equivalents in foreign currency (e.g. balance in foreign currency bank account) are recognised by the principle aforesaid, and these balances are restated in the balance sheet in reporting currency at rate of exchange on balance sheet date. The change in cash

31·3
Closing Date

LSS

or cash equivalents due to exchange gains and losses are, however, not cash flows. This being so, the net increases/decreases in cash or cash equivalents in the cash flow statements are stated exclusive of exchange gains and losses. The resultant difference between cash and cash equivalents as per the cash flow statement and that recognised in the balance sheet is reconciled in the note on cash flow statement.

2.11 DISCLOSURES

AS 3 requires an enterprise to disclose the amount of significant cash and cash equivalent balances held by it but not available for its use, together with a commentary by management. This may happen for example, in case of bank balances held in other countries subject to such exchange control or other regulations that the fund is practically of no use.

AS 3 encourages disclosure of additional information, relevant for understanding the financial position and liquidity of the enterprise together with a commentary by management. Such information may include:

(a) The amount of undrawn borrowing facilities that may be available for future operating activities and to settle capital commitments, indicating any restrictions on the use of these facilities; and

(b) The aggregate amount of cash flows required for maintaining operating capacity, e.g. purchase of machinery to replace the old, separately from cash flows that represent increase in operating capacity, e.g. additional machinery purchased to increase production.

Illustration 1 9:47am

Classify the following activities as (a) Operating Activities, (b) Investing Activities, (c) Financing Activities (d) Cash Equivalents.

(a) *Purchase of Machinery.* → IA

(b) *Proceeds from issuance of equity share capital* → FA

(c) *Cash Sales.* → OA

(d) *Proceeds from long-term borrowings.* → FA

(e) *Cheques collected from Trade receivables.* → OA

(f) *Cash receipts from Trade receivables.* ⇒ OA

(g) *Trading Commission received.* ⇒ OA

(h) *Purchase of investment.* ⇒ IA

(i) *Redemption of Preference Shares.* ⇒ FA

(j) *Cash Purchases.* ⇒ OA

(k) *Proceeds from sale of investment* ⇒ IA

(l) *Purchase of goodwill.* ⇒ IA

(m) *Cash paid to suppliers.* ⇒ OA

(n) *Interim Dividend paid on equity shares.* ⇒ FA

(o) *Wages and salaries paid.* ⇒ OA

(p) *Proceed from sale of patents.* ⇒ IA

(q) *Interest received on debentures held as investment.* ⇒ IA

(r) *Interest paid on Long-term borrowings.* ⇒ FA

(s) *Office and Administration Expenses paid* ⇒ OA

(t) *Manufacturing Overheads paid.* ⇒ OA

(u) *Dividend received on shares held as investments.* ⇒ IA

(v) *Rent Received on property held as investment.* ⇒ IA

(w) *Selling and distribution expense paid.* ⇒ OA

(x) *Income tax paid* ⇒ OA

(y) *Dividend paid on Preference shares.* ⇒ FA

(z) *Underwritings Commission paid.* ⇒ FA

(aa) *Rent paid.* ⇒ OA

(bb) *Brokerage paid on purchase of investments.* → IA

(cc) *Bank Overdraft* → payable on demand → CE; → otherwise → FA

(dd) *Cash Credit* → FA

(ee) *Short-term Deposits* → IA

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(ff) *Highly liquid Marketable Securities (without risk of change in value)* → CE

(gg) *Refund of Income Tax received.* → OA

Solution

(a) Operating Activities: c, e, f, g, j, m, o, s, t, w, x, aa & gg.

(b) Investing Activities: a, h, k, l, p, q, u, v, bb & ee.

(c) Financing Activities: b, d, i, n, r, y, z, cc & dd.

(d) Cash Equivalent: ff.

Illustration 2

X Ltd. purchased debentures of ₹10 lacs of Y Ltd., which are redeemable within three months. How will you show this item as per AS 3 while preparing cash flow statement for the year ended on 31st March, 20X1?

Solution

with insignificant risk of change in value-

As per AS 3 on 'Cash flow Statement', cash and cash equivalents consists of cash in hand, balance with banks and short-term, highly liquid investments*. If investment, of ₹10 lacs, made in debentures is for short-term period then it is an item of 'cash equivalents'.

However, if investment of ₹10 lacs made in debentures is for long-term period then as per AS 3, it should be shown as cash flow from investing activities.

Illustration 3

Classify the following activities as per AS 3 Cash Flow Statement:

(i) *Interest paid by financial enterprise* → OA.

(ii) *Tax deducted at source on interest received from subsidiary company* → IA.

(iii) *Deposit with Bank for a term of two years* → IA.

(iv) *Insurance claim received towards loss of machinery by fire* → IA: Extraordinary.

(v) *Bad debts written off* → Non cash → CFS ×

As per AS 3, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say three months or less from the date of acquisition and is subject to insignificant risk of change in value.

Solution

(i) Interest paid by financial enterprise

Cash flows from operating activities

(ii) TDS on interest received from subsidiary company

Cash flows from investing activities

(iii) Deposit with bank for a term of two years

Cash flows from investing activities

(iv) Insurance claim received against loss of fixed asset by fire

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

(v) Bad debts written off

It is a non-cash item which is adjusted from net profit/loss under indirect method, to arrive at net cash flow from operating activity.

Illustration 4

Following is the cash flow abstract of Alpha Ltd. for the year ended 31st March, 20X1:

Cash Flow (Abstract)

Inflows	₹	*Outflows*	₹
Opening balance:			
Cash	*10,000*	*Payment for Account Payables*	*90,000*
Bank	*70,000*	*Salaries and wages*	*25,000*
Share capital – shares issued	*5,00,000*	*Payment of overheads*	*15,000*
Collection on account of Trade Receivables	*3,50,000*	*Property, plant and equipment acquired*	*4,00,000*
		Debentures redeemed	*50,000*
Sale of Property, plant and equipment	*70,000*	*Bank loan repaid*	*2,50,000*
		Taxation	*55,000*
		Dividends	*1,00,000*
		Closing balance:	

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Illustration 5

Prepare Cash Flow from Investing Activities of M/s. Creative Furnishings Limited for the year ended 31-3-20X1.

Particulars	₹
Plant acquired by the issue of 8% Debentures → x	*1,56,000*
Claim received for loss of plant in fire IA: Extra.	*49,600*
Unsecured loans given to subsidiaries CO	*4,85,000*
Interest on loan received from subsidiary companies CI	*82,500*
Pre-acquisition dividend received on investment made CI	*62,400*
Debenture interest paid FA IA x	*1,16,000*
Term loan repaid FA IA x	*4,25,000*
Interest received on investment IA : CI	*68,000* + 8,200 = 76,200
(TDS of ₹ 8,200 was deducted on the above interest) IA	
Book value of plant sold (loss incurred ₹ 9,600)	*84,000*

SP = 74400 → CI

Solution

Cash Flow Statement from Investing Activities of
M/s Creative Furnishings Limited for the year ended 31-03-20X1

Cash generated from investing activities	₹	₹
Interest on loan received	82,500	
Pre-acquisition dividend received on investment made	62,400	
Unsecured loans given to subsidiaries	(4,85,000)	
Interest received on investments (gross value)	76,200	68 000
TDS deducted on interest	(8,200)	
Sale of plant	74,400	
Cash used in investing activities (before extra ordinary item)		(1,97,700)
Extraordinary claim received for loss of plant		49,600
Net cash used in investing activities (after extra ordinary item)		(1,48,100)

Illustration 5 :- Cash flow from investing activities

LSS

Particulars		Amount	Amount
Unsecured loans given to subsidiaries		(485000)	
Interest on loan from subsidiary company		82500	
Pre-acquisition dividend on investments made		62400	
Gross Interest on Investment	76200		
less: TDS on interest	(8200)	68000	
Proceeds from sale of plant		74400	
Cash flow from investing activities before extraord.		(197700)	
Extraordinary items :- claim received for loss of plant		49600	
Cash used in investing activities after extraord items.		(148100)	(148100)

Note :- Plant acquired by issue of debentures doesnot involve cash flow, hence not presented above.

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Scenario based Question

8. How would the following cash flows be classified in accordance with AS 3?

- Corporate Income Tax paid amounting to ₹ 70 lakhs during the reporting period. →OA
- Payment of advance tax ₹ 8,75,000 out of which ₹ 75,000 was towards capital gains arising on account of sale of assets during the reporting period. 800000 → OA 75000 → IA
- Fixed Deposits withdrawn by customers of State Bank of India ₹ 3 crores. OA

9. Money 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

   Discuss in the context of AS 3 Cash Flow Statement.

10. From the following information of XYZ Limited, calculate cash and cash equivalent as on 31-03-20X2 as per AS 3.

Presentation Homework

Particulars	Amount (₹)
Balance as per the Bank Statement → C.E.	25,000
Cheque issued but not presented in the Bank deduct	(15,000) 10000
Short Term Investment in liquid equity shares of ABC Limited	50,000
Fixed Deposit created on 01-11-20X1 and maturing on 15-04-20X2	75,000
Short Term Investment in highly liquid Sovereign Debt Mutual fund on 01-03-20X2 (having maturity period of less than 3 months)	1,00,000 +

Bank Balance in a Foreign Currency Account in India (Conversion Rate: On the day of deposit ₹ 69/USD as on 31-03-20X2 ₹ 70/USD)	*$ 1,000* ×70 C.E.

70000

180000

11. *Z Ltd. has no Foreign Currency Cash Flow during the reporting period. It held a deposit in a bank in France. The balances as at the beginning of the year and at the end of the year were € 100,000 and € 105,000 respectively. The exchange rate at the beginning of the year was € 1 = ₹ 82, and at the end of the year was € 1 = ₹ 85. The increase in the deposit balance of € 5,000 was on account of interest credited on the last day of the reporting period. The deposit was reported at ₹ 82,00,000 in the opening balance sheet and at ₹ 89,25,000 in the closing balance sheet. You are required to show how these transactions would be presented in the Cash Flow Statement as per AS 3.*

12. *Following is the Balance Sheet of Fox Ltd. You are required to prepare cash flow statement using Indirect Method.*

Particulars	***Note No.***	***31st March,20X2 (₹)***	***31st 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			

Question 11 :- Exchange Difference

While calculating cash flow, exchange gain of ₹ 300000 will be deducted from NPBT as this gain is not realised in cash (non cash item).

Rough P&L

	Exch. Gain 300000
NPBT	

To calculate cash flow, we move in the reverse order of P&L. Hence, EG will now be deducted from NPBT.

While reconciling opening cash and cash equivalents with closing cash and cash equivalents, exchange gain of 3,00,000 will be added.

Opening Cash & Cash Equivalents	: € 1,00,000 × 82	= 82,00,000
+ Interest received (on 31.3.)	: € 5000 × 85	= 4,25,000
+ Exchange difference	: € 1,00,000 × (85 − 82)	= 3,00,000
Closing cash & cash equivalents	= € 1,05,000 × 85	= 89,25,000

Answers to Scenario based Question

8. As per AS 3, the given cash flows shall be recorded as under:

Corporate Income Tax paid amounting to ₹ 70 lakhs during the reporting period.	₹ 70 lakhs: Operating Cash Flows
Payment of advance tax ₹ 8,75,000 out of which ₹ 75,000 was towards capital gains arising on account of sale of assets during the reporting period.	₹ 8,00,000: Operating Cash Flows ₹ 75,000: Investing Cash Flows
Fixed Deposits withdrawn by customers of State Bank of India ₹ 3 crores.	₹ 3 crores: Operating Cash Flows for State Bank of India.

9. Treatment as per AS 3 'Cash Flow Statement'

(i) Loans and advances given and interest earned

(1) to suppliers - Cash flows from operating activities

(2) to employees - Cash flows from operating activities

(3) to its subsidiary companies - Cash flows from investing activities

(ii) Investment made in subsidiary company and dividend received

Cash flows from investing activities

(iii) Dividend paid for the year (Financing / non-financing)

Cash flows from financing activities

10. Computation of Cash and Cash Equivalents as on 31st March, 20X2

	₹
Cash balance with bank (₹ 25,000 less ₹ 15,000)	10,000
Short term investment in highly liquid sovereign debt mutual fund on 1.3.20X2	1,00,000
Bank balance in foreign currency account ($1,000 x ₹ 70)	70,000
	1,80,000

P&L

EG 3L

NP

Note: Short term investment in liquid equity shares and fixed deposit will not be considered as cash and cash equivalents.

11. The Statement of Profit and Loss was credited on account of:

€ 100000 → S, E

100000 → S 82, E 85 — 3 Gain

Interest Income: € 5,000 x ₹ 85 = ₹ 4,25,000

Exchange difference = € 100,000 x (₹ 85 – ₹ 82) = ₹ 3,00,000

x 3 = 300000

CFS

In preparing the Cash Flow Statement, the exchange difference of ₹ 3,00,000 should be deducted from the Net Profit before taxes, since it is a non-cash item. However, in order to reconcile the opening balance of the Cash and Cash Equivalents with its closing balance, the Exchange Difference of ₹ 3,00,000 should be added to the opening balance in a Note to the Cash Flow Statement.,

OA → CF
IA → CF
FA → CF

Cash gen. xxx
Op. C & CE (+)
Cl. C & CE

Cash Flows arising from transactions in a Foreign Currency shall be recorded in Z Ltd.'s reporting currency by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the cash flow.

Op = 100000 x 82 = 8200000
Int = 5000 x 85 = 425000
8625000
Cl. = 105000 x 85 = 8925000

12. **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	8,000	
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)