

- Cash Flow Statement
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## Cash Flow Statement

The Cash Flow Statement is a financial statement that shows the inflows and outflows of cash and cash equivalents during a specific period. The statement is prepared in accordance with Accounting Standard-3 (Revised).

### Key Definitions and Features:

- **Cash and Cash Equivalents:** Assets that are cash or can be converted into cash immediately.
- **Cash Inflows:** Transactions that increase cash and cash equivalents.
- **Cash Outflows:** Transactions that decrease cash and cash equivalents.
- **Accounting Standard-3 (Revised):** Provides guidelines for preparing the Cash Flow Statement.

### Heads of Cash Flows as per AS-3 (Revised):

- Cash Flow from Operating Activities
- Cash Flow from Investing Activities
- Cash Flow from Financing Activities

### Objectives of Preparing Cash Flow Statement:

- To depict sources and uses of cash.
- To facilitate formulation of financial policies such as dividend policy.
- To ascertain the liquidity position of the enterprise.
- To determine the net change in cash and cash equivalents.
- To study trends in cash receipts and payments.

### Benefits of Cash Flow Statement:

- Provides accurate information about cash-based transactions.
- Helps in assessing future cash requirements by comparing past cash budgets.
- Assists management in financial decision-making and prioritizing activities.
- Reveals investing and financing cash transactions and helps evaluate financial structure.
- Helps identify profitability when compared with ratio analysis.

### Practice Set:

- *Level 1 – Easy:* Define Cash Flow Statement and list its three main heads.
- *Level 2 – Moderate:* Explain the objectives of preparing a Cash Flow Statement.
- *Level 3 – Challenging:* Discuss the benefits of Cash Flow Statement for a business.

**Answer Key:**

- Cash Flow Statement shows inflows and outflows of cash and cash equivalents.
- Three main heads: Operating, Investing, and Financing Activities.
- Objectives include depicting cash sources and uses, liquidity assessment, and financial policy formulation.
- Benefits include accurate cash transaction information, future cash planning, and financial structure evaluation.

**Quick Reference:** Cash Flow Statement = Operating + Investing + Financing Activities cash flows.

**Glossary:**

- **Cash Equivalents:** Liquid assets convertible to cash immediately.
- **Liquidity:** Ability to meet short-term obligations.

## Operating Activities

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Operating Activities are the main revenue-generating activities of a business. They include transactions and events that affect net profit or loss.

**Examples of Cash Flow from Operating Activities:**

- Cash sales of goods and services.
- Cash received from customers (trade receivables).
- Cash paid to suppliers (trade payables).
- Payments of operating expenses such as rent, wages, salaries, and taxes.
- Cash received as commission, fees, or royalties.

## Operating Activities

### Cash Inflows

- (i) Cash Sales
- (ii) Cash received from Trade Receivables
- (iii) Cash received as Commission
- (iv) Cash received as Fees
- (v) Cash received as Royalty

**Operating Activities in Financial Companies:** For financial companies, operating activities mainly involve dealing in securities.

- Cash inflows: Interest received, dividends received, sale of securities.
- Cash outflows: Interest paid, purchase of securities.

## Operating Activities

### Cash Inflows

- (i) Cash received for Interest
- (ii) Cash received from Dividends
- (iii) Proceeds from Sale of Securities

#### Practice Set:

- *Level 1 – Easy:* List two examples of cash inflows from operating activities.
- *Level 2 – Moderate:* Explain why operating activities are important for a business.
- *Level 3 – Challenging:* Differentiate between operating activities of manufacturing and financial companies.

#### Answer Key:

- Examples: Cash sales, cash received from customers.
- Operating activities generate revenue and affect net profit.
- Manufacturing companies focus on sales and expenses; financial companies focus on securities transactions.

**Quick Reference:** Operating activities = day-to-day business cash flows.

#### Glossary:

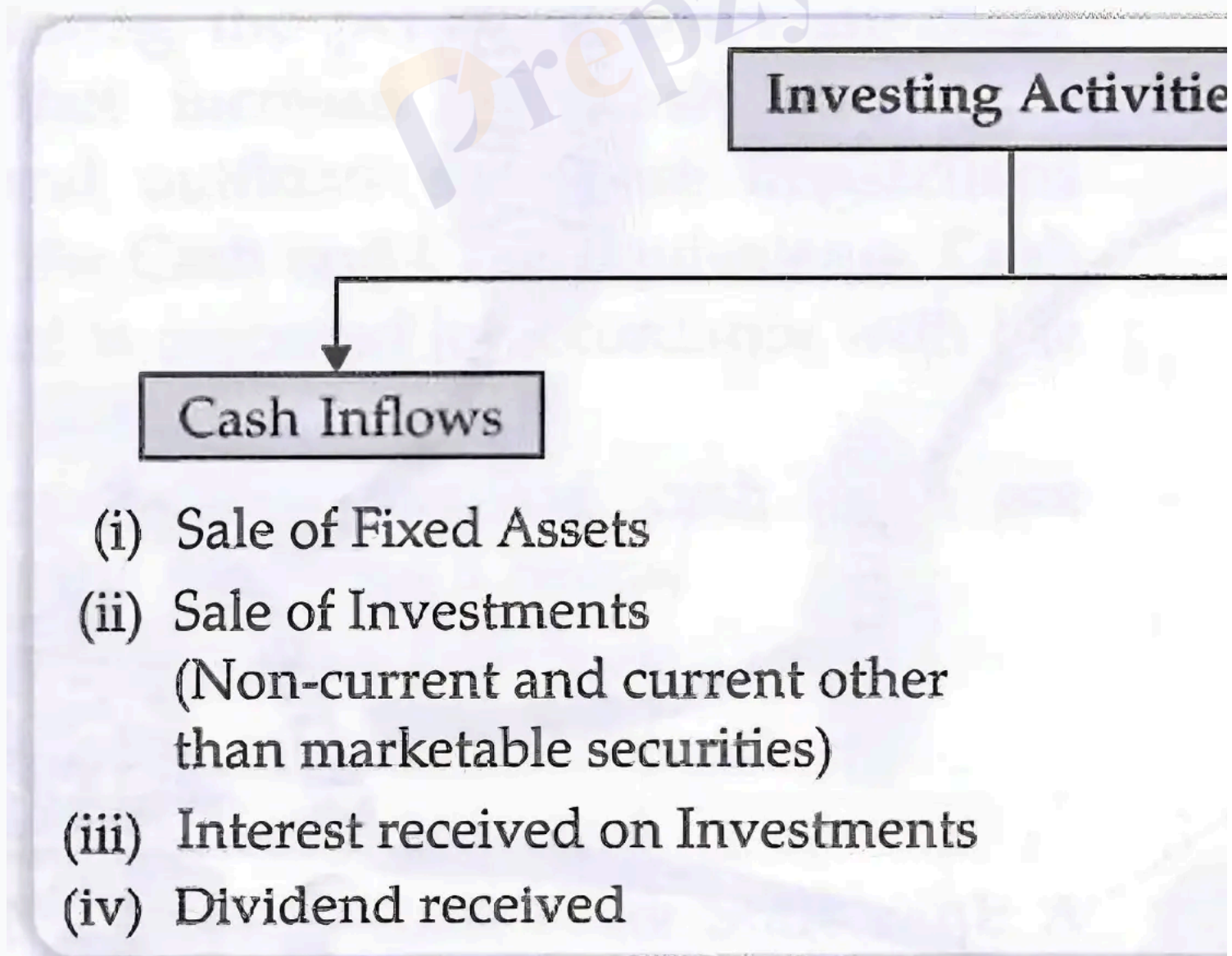
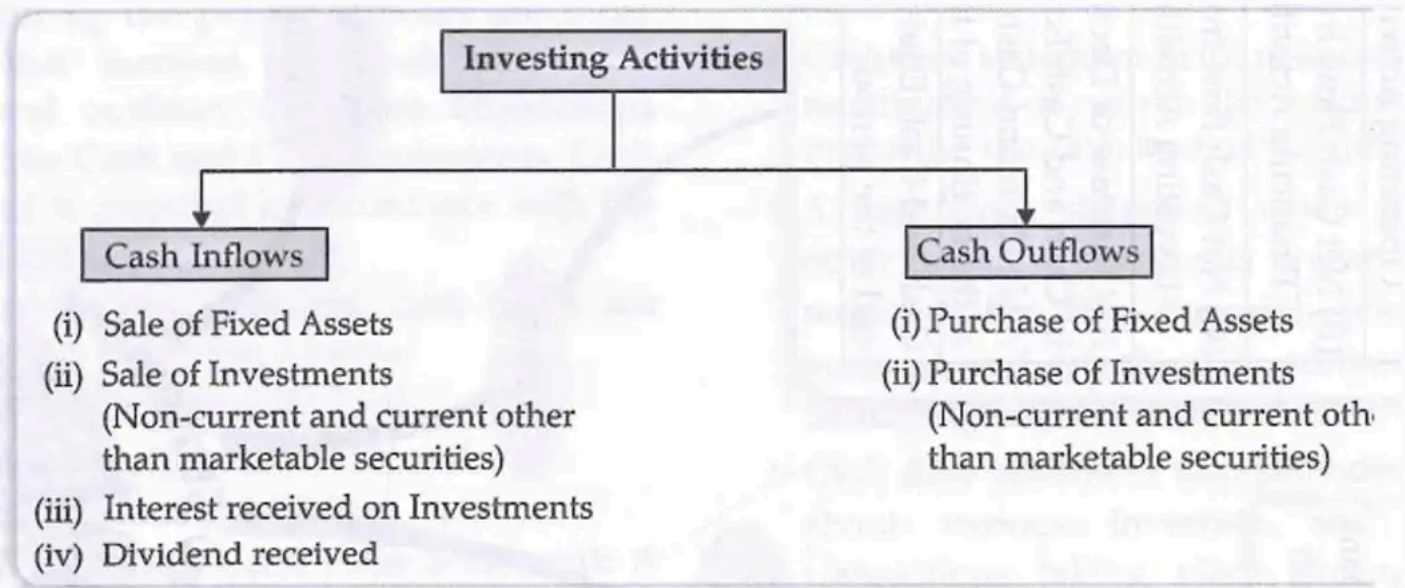
- **Trade Receivables:** Amounts owed by customers.
- **Trade Payables:** Amounts owed to suppliers.

## Investing Activities

Investing Activities relate to acquisition and disposal of long-term assets and other investments not included in cash equivalents.

### Examples of Cash Flow from Investing Activities:

- Cash inflows: Sale of fixed assets, sale of investments, interest received on investments, dividends received.
- Cash outflows: Purchase of fixed assets, purchase of investments.



### Practice Set:

- *Level 1 – Easy:* Define investing activities with two examples.
- *Level 2 – Moderate:* Explain the significance of cash inflows from investing activities.
- *Level 3 – Challenging:* Prepare a simple cash flow calculation from investing activities given asset purchase and sale data.

### Answer Key:

- Investing activities involve buying and selling long-term assets; examples include purchase and sale of machinery.
- Cash inflows indicate recovery of investments and income from investments.
- Net cash flow = Cash received from sale - Cash paid for purchase.

**Quick Reference:** Investing activities = cash flows from asset and investment transactions.

### Glossary:

- **Fixed Assets:** Long-term tangible assets used in business.
- **Investments:** Assets held for earning income or capital appreciation.

## Financing Activities

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Financing Activities result in changes in the size and composition of the owners' capital and borrowings of the business.

### Examples of Cash Flow from Financing Activities:

- Cash inflows: Proceeds from issuing shares, debentures, long-term loans, and bank credit.
- Cash outflows: Repayment of loans, payment of interest and dividends, buyback of shares, redemption of preference shares, repayment

# Financing Activities

## Cash Inflows

- (i) Issue of Shares in Cash (i)
- (ii) Issue of Debentures in Cash (ii)
- (iii) Proceeds from Long-term Loans (iii)
- (iv) Proceeds from Bank Overdraft or Cash Credit (iv)
- (v) (v)
- (vi) (vi)
- (vii) (vii)

### Format of Cash Flow Statement

Cash Flow Statement of \_\_\_\_\_  
for the year ended \_\_\_\_\_  
[As per Accounting Standard (AS-3) (Revised) (Indirect Method)]

Particulars	₹	₹
<b>1. Cash Flow from Operating Activities</b>		
(A) Net Profit before Taxation and Extraordinary Items (WN 1)		.....
Adjustments for Non-cash and Non-operating Items		
(B) Items to be added back:		
Depreciation	.....	
Interest on Borrowings and Debentures	.....	
Goodwill / Patents / Trade Marks/Copyrights Amortised	.....	
Loss on Sale of Fixed Assets	.....	
Increase in Provision for Doubtful Debts	.....	
(C) Items to be Deducted:		
Interest Income	.....	
Dividend Income	.....	
Rental Income	.....	
Profit on Sale of Fixed Assets	.....	
Liability / Provisions written back (Decrease in Provision for Doubtful Debts)	.....	
(D) Operating profit before working capital changes (A + B - C)	.....	
(E) Add: Decrease in Current Assets	.....	
Increase in Current Liabilities	.....	
(F) Less: Increase in Current Assets	(.....)	
Decrease in Current Liabilities	(.....)	
(G) Cash generated from Operations (D + E - F)	.....	
(H) Less: Income tax paid (Net of Refund of Tax)	(.....)	
Net Cash Flow from (or used in) Operating Activities	(X)	.....
<b>2. Cash Flow from Investing Activities</b>		
Proceeds from Sale of Tangible Fixed Assets	.....	
Proceeds from Sale of Intangible Fixed Assets	.....	
Proceeds from Sale of Non-Current Investments	.....	
Interest and Dividend Received (for Non-financial Companies only)	.....	
Rental Income	.....	
Purchase of Tangible Fixed Assets	(.....)	
Purchase of Intangible Assets like Goodwill, Patents, etc.	(.....)	
Purchase of Non-Current Investments	(.....)	
Extraordinary Items (e.g. Insurance claim on Machinery against fire)	(.....)	
Net Cash Flow from (or used in) Investing Activities	(Y)	.....
<b>3. Cash Flow from Financing Activities</b>		
Proceeds from Issue of Share Capital and Debentures	.....	
Proceeds from Long-term Borrowings	.....	
Increase/Decrease in Bank Overdraft and Cash Credit	.....	
Final Dividend Paid	(.....)	
Interim Dividend Paid	(.....)	
Interest on Long-term Borrowings Paid	(.....)	
Redemption of Debentures/Preference Shares	(.....)	
Extraordinary Items (e.g. Buy-back of shares)	(.....)	
Net Cash Flow from (or used in) Financing Activities	(Z)	.....
<b>4. Net Increase/Decrease in Cash and Cash Equivalents (X + Y + Z)</b>		
<b>5. Add: Cash and Cash Equivalents in the beginning of the year (WN 2)</b>		
<b>6. Cash and Cash Equivalents at the end of the year (WN 3)</b>		

- *Level 1 – Easy:* List two cash inflows and two cash outflows from financing activities.
- *Level 2 – Moderate:* Explain the importance of financing activities in cash flow management.
- *Level 3 – Challenging:* Prepare a cash flow statement format using the indirect method for financing activities.

**Answer Key:**

- Inflows: Issue of shares, long-term loans; Outflows: Loan repayment, dividend payment.
- Financing activities provide funds for business growth and capital structure management.
- Format includes listing inflows and outflows, calculating net cash from financing activities.

**Quick Reference:** Financing activities = cash flows related to capital and borrowings.

**Glossary:**

- **Debentures:** Long-term debt instruments issued by companies.
- **Dividend:** Distribution of profits to shareholders.

## Preparation of Cash Flow Statement

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The Cash Flow Statement is prepared using the indirect method as per Accounting Standard-3 (Revised). It involves adjusting net profit for r

**Working Notes:****1. Calculation of Net Profit before Tax and Extraordinary Items:**

Particulars	₹
Net Profit of the current year or Difference between Closing Balance and Opening Balance of Surplus <i>i.e.</i> , Balance in Statement of Profit & Loss	.....
<i>Add:</i> Transfer to reserves (or transfer to reserves from Surplus <i>i.e.</i> , Balances in Statement of Profit & Loss)	.....
Dividend Paid (Proposed Dividend for Previous year)	.....
Interim Dividend paid during the year	.....
Provisions for Tax made during the current year	.....
Extraordinary items if any debited to Statement of Profit & Loss	.....
<i>Less:</i> Refund of tax credited to Statement of Profit & Loss	.....
Extraordinary Items, if any, credited to Statement of Profit & Loss	.....
	.....

**2. Calculation of Cash and Cash Equivalents in the beginning:**

Particulars	₹
Cash in Hand	.....
Cash at Bank	.....
Short-term Deposits	.....
Marketable Securities	.....
Cheques and Drafts in Hand	.....
	.....

**3. Calculation of Cash and Cash Equivalents at the end:**

Particulars	₹
Cash in Hand	.....
Cash at Bank	.....
Short-term Deposits	.....
Marketable Securities	.....
Cheques and Drafts in Hand	.....
	.....

## Example-1

Q. Print Ltd. has given you the following information:

Assets as on April 01, 2016	50,000
Assets as on March 31, 2017	60,000
Accumulated Depreciation on April 01, 2016	25,000
Accumulated Depreciation on March 31, 2017	15,000

During the year, a Assets costing ₹ 25,000 with Accumulated Depreciation of ₹ 15,000 was sold for ₹ 13,000. Calculate cash flow from Investing Activities on the basis of the above information.

Ans. Cash Flows from Investing Activities

Sale of Assets	13,000
Purchase of Assets	(35,000)
Net cash used in Investing Activities	(22,000)

Working Notes:

Assets Account

Dr.			Cr.		
Particulars	J. F.	(₹)	Particulars	J. F.	(₹)
To Balance b/d		50,000	By Cash (proceeds from sale of machine)		13,000
To Statement of Profit and Loss (profit on sale of machine)		3,000	By Accumulated Depreciation		15,000
To Cash (balancing figure: new Assets purchased)		35,000	By Balance c/d		60,000
		<u>88,000</u>			<u>88,000</u>

Accumulated Depreciation Account

Dr.			Cr.		
Particulars	J. F.	(₹)	Particulars	J. F.	(₹)
To Assets		15,000	By Balance b/d		25,000
To Balance c/d		15,000	By Statement of Profit and Loss (Depreciation provided during the year)		5,000
		<u>30,000</u>			<u>30,000</u>

## Example-2

Q. Following is the Balance Sheet of J.M. Ltd. as at 31.03.2016:

**J.M. Ltd.**  
**Balance Sheet as at 31.03.2016**

Particulars	Note No.	31.03.2016 (₹)	31.3.2015 (₹)
<b>I. EQUITY AND LIABILITIES:</b>			
<b>1. Shareholders' Funds:</b>			
(a) Share Capital		2,25,000	1,75,000
(b) Reserves and Surplus	1	1,12,500	56,250
<b>2. Non-Current Liabilities:</b>			
Long-term Borrowings	2	1,12,500	87,500
<b>3. Current Liabilities:</b>			
(a) Short-term Borrowings	3	37,500	18,750
<b>Total</b>		<b>4,87,500</b>	<b>3,37,500</b>
<b>II. ASSETS:</b>			
<b>1. Non-Current Assets:</b>			
<b>(a) Fixed Assets</b>			
(i) Tangible	4	3,66,250	2,28,750
(ii) Intangible	5	25,000	37,500
(b) Non-Current Investments		37,500	25,000
<b>2. Current Assets:</b>			
(a) Current Investments		10,000	17,500
(b) Inventories	6	30,500	18,000
(c) Cash and Cash Equivalent		18,250	10,750
<b>Total</b>		<b>4,87,500</b>	<b>3,37,500</b>

### Notes to Accounts

S. No.	Particulars	31-3-2016 (₹)	31-3-2015 (₹)
1.	<b>Reserves and Surplus</b> Surplus, i.e., Balance in Statement of Profit & Loss	1,12,500	56,250
2.	<b>Long-term Borrowings:</b> 12% Debentures	1,12,500	87,500

3.	<b>Short-term Borrowings:</b> Bank Overdraft	37,500	18,750
4.	<b>Tangible Assets:</b> Machinery Less: Accumulated Depreciation	4,18,750 (52,500)	2,63,750 (35,000)
5.	<b>Intangible Assets:</b> Goodwill	25,000	37,500
6.	<b>Inventories:</b> Stock-in-trade	30,500	18,000
7.	<b>Contingent liabilities:</b> Proposed Dividend	50,000	31,250

### Additional Information:

- (i) ₹ 25,000, 12% debentures were issued on 31.3.2016.
- (ii) During the year a piece of machinery costing ₹ 20,000, on which accumulated depreciation was ₹ 10,000 was sold at a loss of ₹ 2,500.



**Ans. Step 1: Calculation of Net Profit before Tax:**

Net Profit as per Statement of Profit & Loss	₹ 56,250
Add: Dividend Paid	31,250
Net Profit before Tax & Extraordinary Items	<u>87,500</u>

**Step 2: Calculation of machinery purchased during the year**

Dr. Machinery Account Cr.

Particulars	(₹)	Particulars	(₹)
To Balance b/d	2,63,750	By Cash A/c	7,500
To Cash A/c	1,75,000	By Statement of Profit and Loss	2,500
(Purchase Bal. fig.)		By accumulated Depreciation A/c	10,000
		By Balance c/d	4,18,750
	<u>4,38,750</u>		<u>4,38,750</u>

- Step-by-step Explanation:**
- Calculate net profit before tax and extraordinary items by adjusting net profit with dividends, reserves, and taxes.
  - Prepare asset and accumulated depreciation accounts to find cash used or received from asset transactions.
  - Calculate cash flows from operating activities by adjusting net profit for non-cash expenses and working capital changes.
  - Calculate cash flows from investing activities based on asset purchases and sales.
  - Calculate cash flows from financing activities based on changes in capital and borrowings.

**Step 3: Calculation of Accumulated Depreciation charged for the year 2016 to Profit and Loss Account**

Dr. Accumulated Depreciation Account Cr.

Particulars	(₹)	Particulars	(₹)
To Machinery A/c	10,000	By Balance b/d	35,000
To Balance c/d	52,500	By Statement of Profit and Loss	27,500
	<u>62,500</u>	(Balancing Figure)	<u>62,500</u>

- **Level 1 – Easy:** What is the first step in preparing a cash flow statement using the indirect method?
- **Level 2 – Moderate:** Explain how depreciation affects the cash flow from operating activities.

**Step 4:**

- **Level 3 – Challenging:** Prepare a cash flow statement from given balance sheets and profit and loss data.

**Cash Flow Statement of J.M. Ltd for the year ended 31<sup>st</sup> March, 2016 as per AS-3 (Revised)**

Particulars	Amount (₹)	Amount (₹)
<b>Answer Key: Cash Flow from Operating Activities:</b>		
Net Profit before tax & Extraordinary Items (Note 1)	87,500	
Add: Non-cash and non-operating charges:	12,500	
Depreciation on Machinery	27,500	
		<u>1,28,000</u>

**Quick Reference:** Cash Flow Statement = Net Profit ± Non-cash items ± Working Capital changes + Investing + Financing Activities.

**Glossary:**

**Less:** Increase in Current Assets:  
Increase in Inventories

- **Indirect Method:** Preparing cash flow statement by adjusting net profit for non-cash transactions.
- **Working Capital:** Current assets minus current liabilities.

Interest on Debentures	10,500	
Loss on sale of Machinery	2,500	
Operating profit before working capital changes	1,40,500	
		<u>1,28,000</u>
<b>II: Cash Flow from Investing Activities:</b>		
Purchase of Machinery	(1,75,000)	
Sale of Machinery	7,500	
Purchase of Non-Current Investments	(12,500)	
Net Cash used in Investing Activities		<u>(1,80,000)</u>
<b>III: Cash Flow from Financing Activities:</b>		
Issue of Share Capital	50,000	
Issue of 12% Debentures	25,000	
Interest on Debentures paid	(10,500)	
Dividend paid	(31,250)	
Bank Overdraft raised	18,750	
Net Cash flow from Financing Activities		<u>52,000</u>
Net change in cash & cash equivalents (I + II + III)		<u>(Nil)</u>
Add: Opening balance of cash & cash equivalents:		
Current Investments	17,500	
Cash and Cash Equivalents	10,750	<u>28,250</u>

Cash and Cash Equivalents  
Closing Balance of cash & cash equivalents:  
Current Investments  
Cash and Cash Equivalents

	20,000	28,250
	10,000	
	18,250	28,250

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