

# 6

## Cash Flow Statement

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### 1. Introduction

Profit and loss statement and balance sheet are included in financial accounts. Both the statements are prepared for predetermined objectives. Its preparation process is also predetermined. These statements are prepared on mercantile base. Where actual expenses and actual incomes (of respective year - whether paid in cash or not, whether received in cash or not) are recorded in the profit and loss statement. Revenue expenses and revenue incomes are disclosed in profit and loss statement. Equity-liabilities and assets are disclosed in balance sheet.

In brief, profit and loss account which is prepared on mercantile base, shows profitability of the business. Balance sheet provides information about economic solvency.

Besides, profit and loss statement and balance sheet, cash flow statement is also included as a component of financial accounts. Amongst all assets of the business, cash is the most liquid asset. Cash does not give any direct - return, unless it is invested. e.g. you have ₹ 1,00,000 and for one year you have kept it in locker, this will not give you any return. If this ₹ 1,00,000 is deposited in a bank, invested in share or debentures or invested in any other opportunity, would generate interest, dividend or profit. Thus, the investment of cash is very essential creation of reward and earnings.

The sources of cash and application of cash, both the decisions are very important. It is desirable to procure cash from an appropriate source at the same time it is important to invest cash in appropriate opportunity. This information is not disclosed by profit and loss statement and balance sheet. There are different objectives to prepare these statements. What are the sources of cash ? Where cash is invested ? This information is available from cash flow statement. Therefore the preparation of cash flow is mandatory for certain business enterprises. So that investors can take their decisions in appropriate manner.

As per accounting standard 3 disclosure of cash flow statement is mandatory from 1-4-2004 and onwards for certain business enterprises. The disclosure of cash flow statement is mandatory for those business entities whose equity or debt securities are listed or in the process of being listed on the Indian and foreign stock exchanges. As per accounting standard 3, these business enterprises have to prepare the cash flow statements under indirect method.

Under section 2(40) of Companies Act, 2013, the cash flow statement is included in the definition of financial statements.

## 2. Meaning of Terminologies

(1) **Cash flow** : There are two types of cash flows : (a) cash inflow and (b) cash outflow. Here cash flow means receipt-payment of cash and cash equivalent. A transaction due to which cash or cash equivalent increases is known as cash inflow. A transaction due to which cash or cash equivalent decrease is known as cash outflow.

The difference of cash inflow and cash outflow is called as net cash flow. This difference can be as follows :

		₹
●	Cash inflow	✓ 1,00,000
	Less : Cash outflow	✓ 85,000
	Net cash inflow	✓ 15,000
●	Cash inflow	✓ 85,000
	Less : Cash outflow	✓ 1,00,000
	Net cash outflow	✓ (15,000)

(2) **Cash** : Cash means cash on hand, bank balance.

(3) **Cash equivalent** : Cash equivalent means,

- highly liquid short-term investments
- such investments which can be quickly and with accurate estimated price convertible into cash
- The investment in which the risk of changes in the price is very rare.

e.g. (i) Government securities (ii) Any securities having above stated features.

(4) **Cash flow statement** : Three types of activities are disclosed in cash flow statement.

– Operating activities – Investing activities – Financing activities

There can be cash inflow and/or cash outflow in each activity. The opening balance of cash and cash equivalent is added to cash flows generated through these three activities. At the end whatever amount would arrive will be closing balance of cash and cash equivalent. Cash flow generated from these activities can be positive or negative.

## 3. Classification of Cash Flow Activities :

### Profit and Loss Account

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
Opening stock		Operating incomes	
Purchase			
Purchase expenses		Non-operating incomes →	will be deducted from operating profit
Operating expenses in cash			
Non-cash operating expenses →	Will be added to operating profit		
Financial expenses and appropriation →			
Net profit			

### Balance Sheet

Equity-Liabilities	Amt. (₹)	Assets	Amt. (₹)
Shareholders' funds	Financial activities	Non-current assets	Investing activities
Non-current liabilities			
Current liabilities		Current assets	

Operating activities

In cash flow statement, activities of specific period are classified into three categories :

- (1) Operating activities and cash flow from operating activities
- (2) Investing activities and cash flow from investing activities
- (3) Financing activities and cash flow from financing activities

Their detailed explanation is as follows :

#### (1) Operating activities and cash flow from operating activities :

**Operating activities** : Operating activities are activities that emerge from profit and loss statement. Transactions recorded in profit and loss statements are classified for these activities. In this context operating expenses related discussion is done in the previous chapter of ratio analysis. Operating profit is computed as follows :

**Definition** : "Operating activities means main activities of business to earn income, which are neither investing activities nor financing activities.

These are those activities on the basis of which main income of the business is created.

The identification of operating activities is determined on the basis of the nature of industry of a business unit. The identification of operating activities of each business is based on the nature of business. This discussion is pertaining to main activities of income generation. e.g.

(1) **Trading Company** : For this kind of company, activities of purchase - sales of goods are main activities of income generation.

(2) **Insurance Company** : For this kind of company premium income and payment of claims are main activities of income generation.

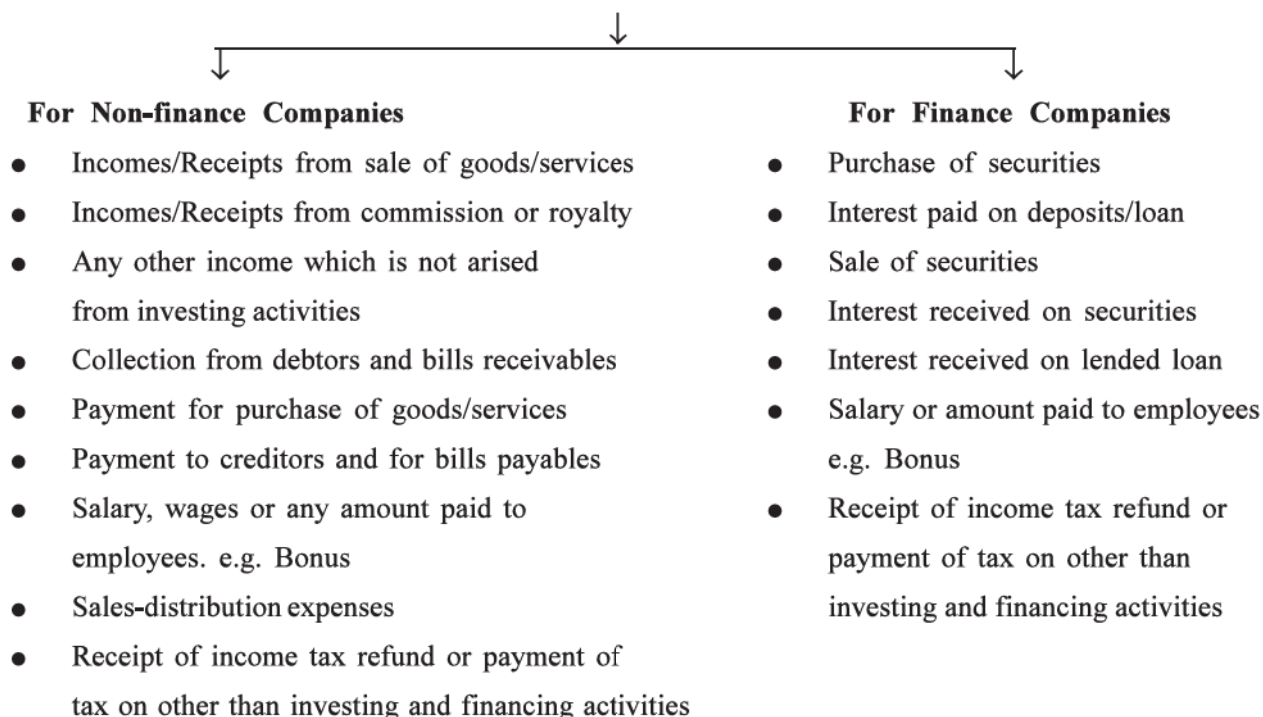
(3) **Bank** : For this kind of business unit lending of loan and acceptance of deposits are main activities of income generation.

Generally by dividing forms of company into two categories, clarity can be obtained.

- (1) Non-finance companies
- (2) Finance companies

The cash flow emerging given the operating activities of both the types of companies can be narrated as under :

### Cash Flow from Operating Activities



**Illustration 1 :** Identify operating activities from the following transactions of Meena Company.

- |                             |                                       |
|-----------------------------|---------------------------------------|
| (1) Salary paid             | (2) Wages paid                        |
| (3) Loan borrowed           | (4) Debentures redeemed               |
| (5) Received from debtors   | (6) Paid for bills payables           |
| (7) Sale of machine on cash | (8) Brokerage received                |
| (9) Purchase of furniture   | (10) Interest received on investments |
| (11) Paid interest on loan  | (12) Income tax refund                |

**Ans. :**

No.	Transactions	Explanation
(1)	Salary paid	Operating activity - Transaction of profit and loss statement
(2)	Wages paid	Operating activity - Transaction of profit and loss statement
(3)	Loan borrowed	Not operating activity - Transaction of equity and liabilities
(4)	Debentures redeemed	Not operating activity - Transaction of equity and liabilities
(5)	Received from debtors	Operating activity - Debtors are arised from sales Sales is operating activity.
(6)	Paid for bills payables	Operating activity - Bills payables arised from creditors and creditors from credit purchase - Purchase is operating activity.
(7)	Sale of machine on cash	Not operating activity - Transaction of assets
(8)	Brokerage received	Operating activity - Transaction of profit and loss statement



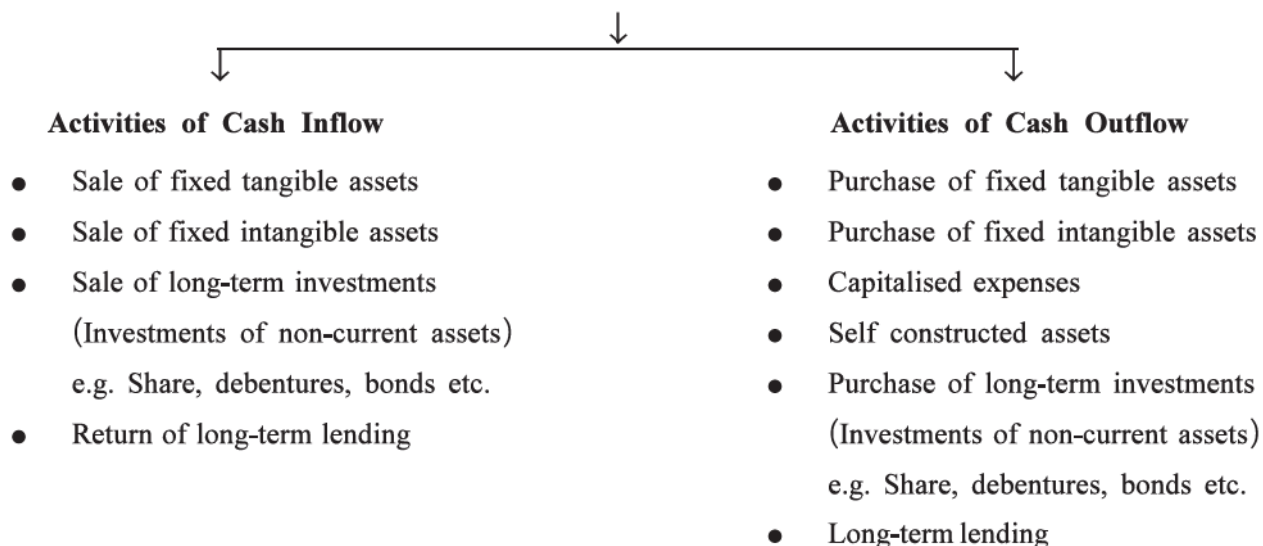
(9)	Purchase of furniture	Not operating activity - Transaction of assets
(10)	Interest received on investments	Not operating activity - Investments are assets. Interest arised on it is part of investment. Transaction of assets
(11)	Paid interest on loan	Not operating activity - Loan is liability. It's paid interest is result of liability. Transaction of equity and liabilities
(12)	Income tax refund	Operating activity - (When no clarification is provided whether it is refund of financing or investing activity, will be treated as operating activity.)

**Note :** There are certain transactions which are always included in operating activities. e.g. Salary, wages, bonus to workers, employees welfare expenses etc.

## (2) Investing Activities :

Investing activities, arise from transactions of assets side of balance sheet. Investing activities means purchase-sale of long-term investments and other investments. Cash and cash equivalent are not included. Long-term assets are those assets which are not acquired for sale purpose. They are used for business activities. Purchase of such assets is treated as cash out flow and sale is treated as cash inflow. e.g. land-building, machines, furniture and other assets held for the generation of income are also included in investing activities. The income received due to these investments like interest, dividend or rent is also included in investing activities.

### Cash Inflow and Outflow of Investing Activities



**Illustration 2 :** From the following transactions of Rita Company identify investing activities. Also state whether the respective activity is cash inflow or cash outflow :

- |                                   |                                 |
|-----------------------------------|---------------------------------|
| (1) Purchase of land              | (2) Sale of machine             |
| (3) Purchase of shares of X co.   | (4) Sale of debentures of Y co. |
| (5) Assets constructed in factory | (6) Purchase of copy-rights     |
| (7) Salary paid                   | (8) Carriage inward paid        |

Ans. :

No.	Transaction	Explanation
(1)	Purchase of land	Investing activity of cash outflow. Investment in asset is increased.
(2)	Sale of machine	Investing activity of cash inflow. Investment is reduced from assets.
(3)	Purchase of shares of X co.	Investing activity of cash outflow. Investment in assets is increased.
(4)	Sale of shares of Y co.	Investing activity of cash inflow. Investment is reduced from assets.
(5)	Assets constructed in factory	Investing activity of cash outflow. Investment is increased in assets.
(6)	Purchase of copy-rights	Investing activity of cash outflow. Investment is increased in assets.
(7)	Salary paid	Not investing activity. (Operating activity of cash outflow.)
(8)	Carriage inward paid	Not investing activity. (Operating activity of cash outflow.)

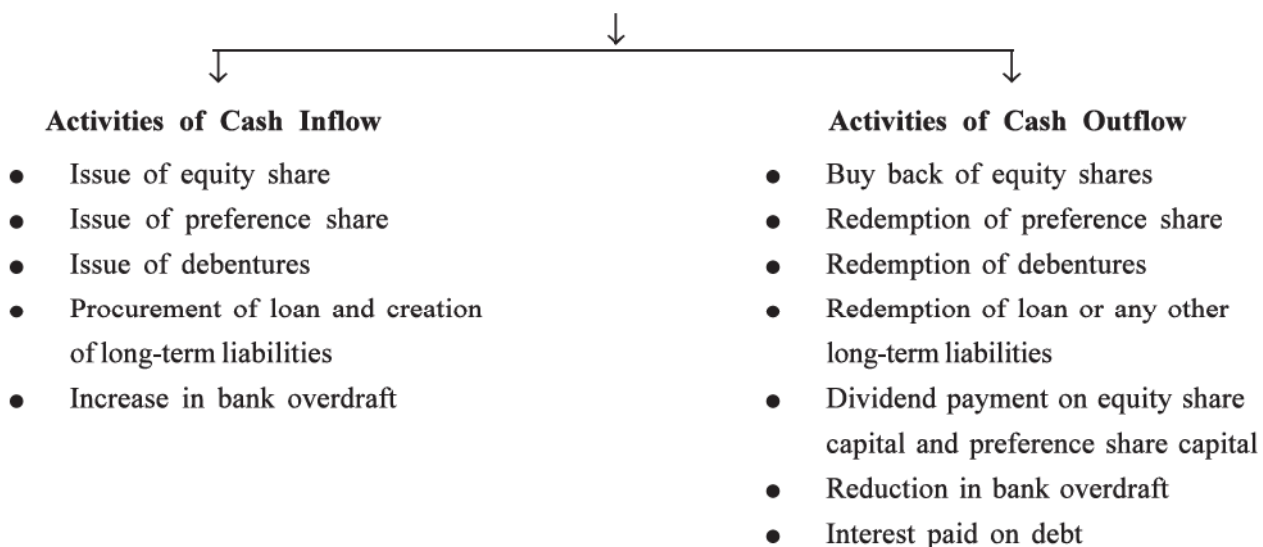
**Note :** There are certain transactions which are always included by investing activities for purchase of fixed (non-current) asset. (Investment in fixed assets) is not done for resale purpose. Thus these transactions are always considered as investing activities. e.g. purchase of patent, purchase of furniture etc. During transaction if cash/bank A/c is debited will be treated as cash inflow and if cash/bank A/c is credited will be treated as cash outflow.

### (3) Financing Activities :

Financing activities, arise from the transactions of equity and liabilities (except those of current liabilities) side of balance sheet. "Financing activities are such activities due to which size and/or composition of owners' capital (including preference share capital) and borrowed capital of business get changed."

Financing activities have relation with increase or decrease of equity share capital, preference share capital, debentures, loan etc. It means that the increase in long-term owners' capital and borrowed capital shows cash inflow and their reduction shows cash outflow of financing activities.

#### Cash Inflow and Cash Outflow of Financing Activities



**Illustration 3 :** From the following transactions of Nayana Company identify financing activities. Also state whether the respective activity is cash inflow or cash outflow.

- |                                    |  |
|------------------------------------|--|
| (1) Redemption of preference share | (2) Issue of debentures                |
| (3) Payment of dividend            | (4) Loan borrowed for 3 years from BOB |
| (5) Sale of machine                | (6) Wages paid                         |
| (7) Commission received            | (8) Interest received on investments   |

**Ans. :**

No.	Transactions	Explanation
(1)	Redemption of preference share	Financing activity of cash outflow. It reduces capital.
(2)	Issue of debentures	Financing activity of cash inflow. It increases liabilities.
(3)	Payment of dividend	Financing activity of cash outflow. Dividend paid in share capital. Thus it is financing activity.
(4)	Loan borrowed for 3 years from BOB	Financing activity of cash inflow. Liability is increased.
(5)	Sale of machine	Not financing activity. (Investing activity of cash inflow.)
(6)	Wages paid	Not financing activity. (Operating activity of cash outflow.)
(7)	Commission received	Not financing activity. (Operating activity of cash inflow.)
(8)	Interest received on investments.	Not financing activity. (Interest received on investments is investing activity of cash inflow.)

**Note :** There are certain transactions which are always included in financing activities. e.g. Dividend paid on share capital. This transaction is linked with capital, thus considered as financing activity.

#### 4. Special Activities :

(1) **Two activities from one transaction :** Two types of payments are included in each instalment of hire purchase - payment towards principal amount and interest amount.

- |   |   |
|---|---|
| ● Payment towards principal<br>(Payment towards cash price) | ● It is investing activity. Value of assets is increased. Investing activity of cash outflow.     |
| ● Interest payment  | ● It is return of liability, thus it is a financing activity. Financing activity of cash outflow. |

(2) **Cash transaction but no cash inflow - outflow :**

- |                          |  |
|--------------------------|--|
| Cash deposited with bank | → cash reduced, bank balance increased |
| Cash withdrawn from bank | → cash increased, bank balance reduced |

Cash balance and bank balance are shown at the same place in cash flow statement. It is known as cash and cash equivalent. This transaction has relation with cash, but does not influence cash and cash equivalent.

(3) **Non-cash transactions and provisions :** Many transactions of business are not done in cash form. Thus during preparation of cash flow these transactions are not considered as cash flow. e.g. Depreciation charged on tangible assets, amount amortized on intangible assets, issue of equity share and debenture without cash consideration, conversion of debentures into equity.

**Illustration 4 :** Following transactions of Bharati Company classified into operating, investing and financing activities.

- |                              |  |
|------------------------------|--|
| (1) Issue of equity share    | (2) Redemption of preference share         |
| (3) Long-term loan from bank | (4) Cash balance                           |
| (5) Bank balance             | (6) Quickly saleable short-term securities |

- |                                  |  |
|----------------------------------|--|
| (7) Short-term bank deposit      | (8) Commission received                    |
| (9) Amount received from debtors | (10) Payment to creditors                  |
| (11) Sale of machine             | (12) Purchase of furniture                 |
| (13) Manufacturing expenses      | (14) Commission paid                       |
| (15) Income tax paid             | (16) Purchase of investments (Non-current) |
| (17) Sales-distribution expenses | (18) Factory expenses                      |
| (19) Paid for trademark          | (20) Paid for goodwill                     |
| (21) Dividend payment            | (22) Interest received                     |
| (23) Income tax refund           | (24) Purchase of raw material              |
| (25) Rent received               | (26) Rent paid                             |

**Ans. :**

No.	Activities	Transaction Number
(1)	Operating activity	8, 9, 10, 13, 14, 15, 17, 18, 23, 24, 26
(2)	Investing activity	11, 12, 16, 19, 20, 22, 25
(3)	Financing activity	1, 2, 3, 21
(4)	Cash and cash equivalent	4, 5, 6, 7

No.	Transaction	Explanation	Cash Flow
(1)	Issue of equity share	Financing activity	Cash inflow
(2)	Redemption of preference share	Financing activity	Cash outflow
(3)	Long-term loan from bank	Financing activity	Cash inflow
(4)	Cash balance	Non-financing activity	Cash equivalent
(5)	Bank balance	Non-financing activity	Cash equivalent
(6)	Quickly saleable short-term securities	Non-financing activity	Cash equivalent
(7)	Short-term bank deposit	Non-financing activity	Cash equivalent
(8)	Commission received	Operating activity	Cash inflow
(9)	Amount received from debtors	Operating activity	Cash inflow
(10)	Payment to creditors	Operating activity	Cash outflow
(11)	Sale of machine	Investing activity	Cash inflow
(12)	Purchase of furniture	Investing activity	Cash outflow
(13)	Manufacturing expenses	Operating activity	Cash outflow
(14)	Commission paid	Operating activity	Cash outflow
(15)	Income tax paid	Operating activity	Cash outflow
(16)	Purchase of investments (Non-current)	Investing activity	Cash outflow



No.	Transaction	Explanation	Cash Flow
(17)	Sales-distribution expenses	Operating activity	Cash outflow
(18)	Factory expenses	Operating activity	Cash outflow
(19)	Paid for trademark	Investing activity	Cash outflow
(20)	Paid for goodwill	Investing activity	Cash outflow
(21)	Dividend payment	Financing activity	Cash outflow
(22)	Interest received	Investing activity	Cash inflow
(23)	Income tax refund	Operating activity	Cash inflow
(24)	Purchase of raw material	Operating activity	Cash outflow
(25)	Rent received	Investing activity	Cash inflow
(26)	Rent paid	Operating activity	Cash outflow

### 5. The Cash Flow Statement

The cash flow statement provides information about generation of cash flow from different activities. Cash flow is disclosed in terms of cash inflow and cash outflow. As discussed earlier cash inflow and outflow is determined on the basis of different activities.

Where (1) Cash flow from operating activities

(Prepared on the basis of profit and loss statement and profit and loss appropriation. Besides this, changes (increase/decrease) in current assets and current-liabilities are considered.)

(2) Cash flow from investing activities

(Prepared on the basis of assets side of balance sheet and non-operating incomes of profit and loss statement.)

(3) Cash flow from financing activities

(Prepared on the basis of equity and liabilities side of balance sheet, profit and loss statement and profit and loss appropriation.)

#### ● The Format of Cash Flow Statement (Indirect Method) :

**The Cash Flow Statement for ..... Co. Ltd. for the Year Ending on .....**

Particulars	(₹)	(₹)
<b>A</b> Cash flow from operating activities		✓
Net profit of current year		
<b>Less : Non-operating incomes</b>		
Profit on sale of investments	✓	
Profit on sale of assets	✓	
Interest received on investments	✓	
Dividend received on investments	✓	
Rent income on assets	✓	✓
		✓

Particulars	(₹)	(₹)
<b>Add : Non-cash transactions, provisions and financial expenses :</b>		
Depreciation written off	✓	
Intangible assets amortized	✓	
Fictitious assets written off	✓	
Loss on sale of asset	✓	
Taxation provision (of current year)	✓	
Transfer to general reserve	✓	
Proposed dividend (of current year)	✓	✓
<b>Add : Financing expenses</b>		✓
Dividend paid	✓	
Interest paid	✓	✓
Operating profit before changes in working capital		✓
Add : Decrease in current assets	✓	
Increase in current liabilities	✓	✓
		✓
Less : Increase in current assets	✓	
Decrease in current liabilities	✓	✓
		✓
Less : Tax paid of previous year		✓
Cash flow from operation		✓
<b>B Cash flow from investing activities :</b>		
Sale of assets (Tangible - Intangible)	✓	
Sale of non-current investments	✓	
Interest and dividend received	✓	
Rent received	✓	
Purchase of assets (Tangible - Intangible)	(✓)	
Purchase of non-current investments	(✓)	✓
Net cash flow from investing activities		✓
<b>C Cash flow from financing activities :</b>		
Issue of share - debentures	✓	
Proceeds from long-term borrowings	✓	
Short-term borrowings		
(i) Increase in bank overdraft and cash credit	✓	
(ii) Decrease in bank overdraft and cash credit	(✓)	
Payment of final dividend	(✓)	
Payment of interim dividend	(✓)	
Repayment of loan	(✓)	
Redemption of debentures / preference share	(✓)	
Interest paid on debentures / loan	(✓)	
Net cash flow from investing activities		✓
Net interest / decrease in cash - cash equivalent (A+B+C)		✓
Add : Cash - cash equivalent in the beginning of the year		✓
Cash - cash equivalent at the end of the year		✓

**Note :** Figures shown in ( ) are cash outflow.

From the following format of cash flow statement given on page no. 258 and 259, it can be ascertained that this statement is based on three activities. The information for each activity is as follows :

#### 6. Cash Flow from Operating Activities :

Cash flow from operating activities is prepared on the basis of

- (A) Details of profit and loss statement and appropriation of profit
- (B) Changes in current assets and current liabilities (changes in working capital)

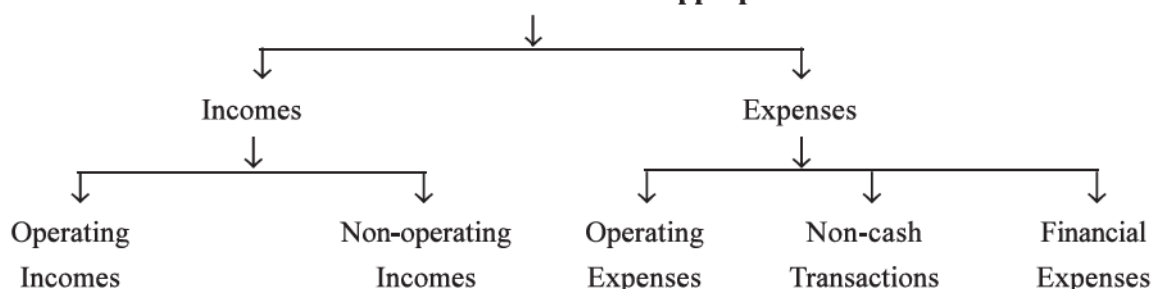
The cash flow from operating activities means the cash flow generated from the day to day transactions of a business entity.

#### (A) Details of Profit and Loss Statement and Appropriation of Profit :

Along with details of profit and loss statement, details of profit and loss appropriation are also included. Profit and loss appropriation statement is an extended form of profit and loss statement.

Details of this statement can be classified as follows :

#### Details of Profit and Loss Statement and Appropriation of Profit



The difference of above stated incomes and expenses is known as profit. In this profit non-operating incomes, non-cash transactions and financial transactions are included :

- Due to non-operating incomes profit increases (are added).
- Due to non-cash transactions profit decreases (are deducted).
- Due to financial expenses profit decreases (are deducted).

To determine cash flow from operating activities the above stated items of profit and loss statement will be given reverse effect.

Cash flow from operating activities is determined as follows :

Profit of current year as per profit and loss statement		✓
Less : Non-operating incomes	✓	
Add : Non-cash transactions (expenses) and appropriation	✓	
Add : Financial expenses	✓	✓
Cash flow generated from operating activities before the changes in working capital.		✓
		✓

#### ● What are Non-operating Incomes :

These are such incomes which do not arise from the business in which company deals. They are not a part of operating profit. Thus they are not considered for computation of cash flow.

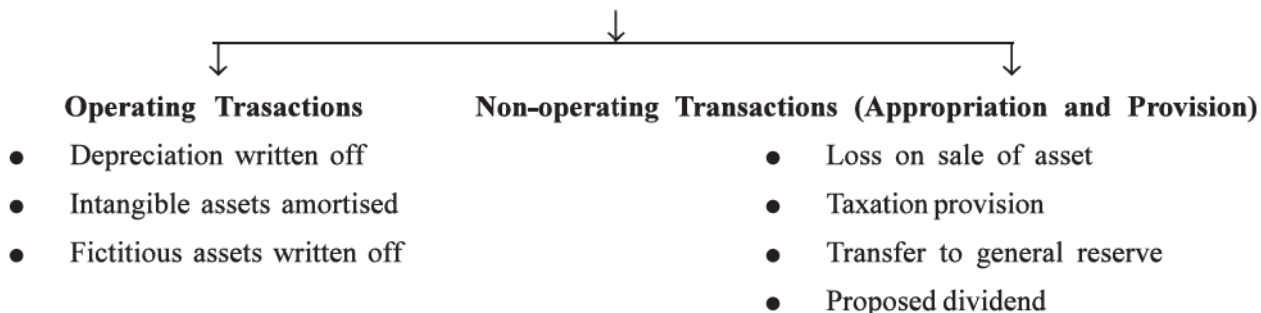
e.g. Profit on sale of investments, profit on sale of assets, interest on investments, dividend received on investments, rent for properties.

These kind of incomes are not considered to determine cash flow from operating activities during preparation of cash flow statement. These transactions are added in profit and loss statement. Thus, are deducted.

● **What are non-cash transactions, appropriation and provisions ?**

There are two types of non-cash transactions. These transactions are generally considered in reference to expenses.

**Non-cash Transactions, Appropriation and Provisions**



These kind of transactions do not generate cash flow (receipt / payment). Thus to determine cash flow from operating activities of cash flow statement, these are ignored. All these transactions will be added back because, these were debited to profit and loss account (statements).

● **What are the financial expenses ?**

Amounts which are paid as a return of capital are financial expenses. Capital is of two types : Owners capital and borrowed capital. Dividend is paid on equity share capital and preference share capital which are owners' capital while interest is paid on debt. Dividend and interest are expenses of capital. Thus it is financial expense. Thus to determine cash flow from operating activities of cash flow statement, these are ignored. Those are deducted from profit and loss statement and appropriation, so they are to be added back.

**(B) Changes in Current Assets - Current Liabilities (Working Capital)**

During determination of cash flow from operating activities, the effect of changes in current assets and current liabilities i.e. the working capital is considered. The effect of the increase-decrease in current assets and current liabilities is recorded here.

**Note :** Cash and cash equivalent are not included in current assets. It's separate effect is given in the cash flow statement.

**Relation of Cash and Cash Equivalent with Current Assets and Current Liabilities :** Current assets and cash and cash equivalent has inverse relation. Increase in current assets leads to, decrease in cash and cash equivalent, decrease in current assets leads to, increase in cash and cash equivalent.

Current liabilities and cash and cash equivalent has direct relation. Increase in current liabilities, leads to increase in cash and cash equivalent, decrease in current liabilities leads, decrease in cash and cash equivalent.

e.g. opening balance of debtors was ₹ 50,000 and at the end of the year it was ₹ 75,000.

**Explanation :** In the opening of year ₹ 50,000 was invested in debtors and at the end it is increased to 75,000. The investment is increased by ₹ 25,000. Thus cash and cash equivalent (means cash balance or bank balance) would reduce. This is cash outflow. If opening balance of debtors was ₹ 75,000 and at the end it was ₹ 50,000, it means that the investment in debtors is reduced. Consequently cash or cash equivalent would increase, this is cash inflow. Current liabilities have opposite effect. Opening balance of creditors was ₹ 50,000 and at the end of the year it is ₹ 75,000.



Investment would reduce by ₹ 25,000 and thus cash and cash equivalent would increase. This is cash inflow. If opening balance of creditors was ₹ 75,000 and at the end of the year it is ₹ 50,000, the investment would reduce by ₹ 25,000 and this cash and cash equivalent would reduce. This is cash outflow.

**Effect of increase/decrease in current assets and current liabilities on operating cash flow**

No.	Particulars	Effect on Working Capital	Effect on Cash Flow
1.	Increase in current assets	Increase	Difference will be cash outflow.
2.	Decrease in current assets	Decrease	Difference will be cash inflow.
3.	Increase in current liabilities	Decrease	Difference will be cash inflow.
4.	Decrease in current liabilities	Increase	Difference will be cash outflow.

Stages for computation of cash flow from operating activities :

- (1) Ascertain the difference of closing balance and opening balance of profit and loss account or reserve and surplus. Show this difference as a first item of statement. It is profit of current year.
- (2) Add all non-cash transactions to profit of current year, stated in above (1).
- (3) Add all financial expenses to profit of current year, stated in above (1).
- (4) Deduct all non-operating incomes from profit of current year stated in above (1).
- (5) Also consider adjustments (additional information) if it influences the operating cash flow.

**Note :**

- (1) The following details are disclosed in profit and loss statement :

- Revenue incomes not received in cash
- Revenue expenses not paid in cash
- Depreciation on fixed assets
- Intangible assets amortized and fictitious assets written off
- Profit/loss on sale of non-current assets (investing activity)
- Interest on non-current liability (financing activity)
- Appropriation to reserves and provisions
- Appropriation - payment of dividend (financing activity)

In spite of having disclose of those transactions in profit and loss statements, they do not have influence on cash flow from operating activities. Their special effect is incorporated in cash flow statement.

- (2) Creditors and bills payables (current liabilities) emerge from credit purchase and debtors and bills receivables (current assets) emerge from credit sales.

So current assets and current liabilities are result of operating activities, therefore changes in their size have taken place during the current year, will be disclosed under cash flow from operating activities.

**Illustration 5 :** From the following transactions of Khushbu Company Ltd., calculate cash flow from operating activities.

Particulars	(₹)
Profit before taxes	1,32,000
Goodwill written off	28,000
Patent amortized	17,000
Depreciation wrtitten off	29,000
Transfer to general reserve	23,000
Interest received	12,000
Dividend received	9000
Interest paid	11,000
Dividend paid	25,000
Profit on sale of investments	13,000
Loss on sale of furniture	18,000

**Ans. :**

Therefore, computed amount is profit (cash flow) from operating activities before changes in working capital. In this question no information is provided for current assets and current liabilities.

**Cash Flow from Operating Activities**

Particulars	(₹)	(₹)
Profit before taxes		1,32,000
Add : Non-cash expenses, appropriation and provisions :		
Goodwill written off	28,000	
Patent amortized	17,000	
Depreciation written off	29,000	
Transfer to general reserve	23,000	
Interest paid	11,000	
Dividend paid	25,000	
Loss on sale of furniture	18,000	1,51,000
		2,83,000
Less : Non-operating incomes :		
Interest received	12,000	
Dividend received	9000	
Profit on sale of investments	13,000	34,000
Profit (cash flow) before changes in working capital		2,49,000

**Illustration 6 :** From the following information of Ami Company, calculate cash flow from operating activities.

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
Profit and loss A/c	89,000	64,000
General reserve	34,000	18,000
Taxation provision	22,000	23,000
Depreciation	28,000	16,000
Goodwill	15,000	19,000
Debtors	38,000	18,000
Creditors	45,000	22,000
Bills receivable	8000	12,000
Bills payables	9000	15,000

**Ans. :**

**Cash Flow from Operating Activities for the Year Ending On 31-3-2017**

Particulars	(₹)	(₹)
Closing balance of profit and loss A/c	89,000	
<b>Less :</b> Opening balance of profit and loss A/c	64,000	
Profit of current year		25,000
<b>Add :</b> Non-cash expenses and provisions :		
General reserve	16,000	
Taxation provision (of current year)	22,000	
Depreciation (28,000 – 16,000)	12,000	
Goodwill written off (19,000 – 15,000)	4000	54,000
		79,000
<b>Less :</b> Non-operating incomes :		—
Profit (cash flow) before changes in working capital		79,000
<b>Add :</b> Decrease in current assets : Bills receivables	4000	
Increase in current liabilities : Creditors	23,000	27,000
		1,06,000
<b>Less :</b> Increase in current assets : Debtors	20,000	
Decrease in current liabilities : Bills payables	6000	26,000
		80,000
<b>Less :</b> Income-tax paid of previous year		23,000
<b>Cash flow from operating activities</b>		<b>57,000</b>

**Illustration 7 :** From the following information and balance sheets of two years of Nirav Company, calculate cash flow from operating activities.

### Balance Sheets as at 31-3-2016 and 31-3-2017

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
<b>I Equity and Liabilities :</b>		
<b>(1) Shareholders' funds :</b>		
(a) Share capital	5,00,000	3,00,000
(b) Profit and loss A/c	4,50,000	3,00,000
<b>(2) Non-current liabilities</b>		
12 % debentures	3,00,000	2,00,000
<b>(3) Current liabilities :</b>		
(a) Bank overdraft	40,000	60,000
(b) Trade payables (Creditors)	60,000	90,000
(c) Short-term provisions : Proposed dividend	50,000	30,000
Taxation provision	50,000	40,000
<b>Total</b>	<b>14,50,000</b>	<b>10,20,000</b>
<b>II Assets :</b>		
<b>(1) Non-current assets :</b>		
(a) Fixed assets		
(i) Tangible assets	8,00,000	4,00,000
(ii) Intangible assets	4,50,000	3,20,000
<b>(2) Current assets</b>	2,00,000	3,00,000
<b>Total</b>	<b>14,50,000</b>	<b>10,20,000</b>

**Additional information :**

Interim dividend paid ₹ 20,000.

New debentures are issued at the end of year.



Ans. :

**Cash Flow from Operating Activities for the Year Ending on 31-3-2017**

Particulars	(₹)	(₹)
Closing balance of profit and loss statement	4,50,000	
<b>Less :</b> Opening balance of profit and loss statement	3,00,000	
Difference of profit and loss statement		1,50,000
<b>Add :</b> Non-cash expenses (provisions)		
Proposed dividend (of current year)	50,000	
Taxation provision (of current year)	50,000	
Interim dividend (provisions)	20,000	
Debenture interest	24,000	
		1,44,000
		2,94,000
<b>Less :</b> Non-operating income		—
<b>Operating profit before changes in working capital</b>		<b>2,94,000</b>
<b>Add :</b> Decrease in current assets	1,00,000	
Increase in current liabilities	—	1,00,000
		3,94,000
<b>Less :</b> Increase in current assets	—	
Decrease in current liabilities : Trade payables	30,000	30,000
		<b>3,64,000</b>
<b>Less :</b> Payment of income tax		40,000
<b>Cash flow from operating activities</b>		<b>3,24,000</b>

**Explanation :**

- (1) Interim dividend is given as additional information. Thus it will be paid after it is provided for. This additional information will have two effects.
  - (a) Provision of interim dividend will be added to profit.
  - (b) Interim dividend will be added in financial activities as cash outflow.
- (2) Owners' funds and non-current liabilities of equity and liabilities side are components of financing activities. This will not be reported in cash flow from operating activities.
- (3) All current liabilities excluding provisions will be shown as current liabilities in cash flow from operating activities.
- (4) Under the head of current liabilities the proposed dividend and the taxation provision of the current year are added to profit to determine the cash flow from operating activities. A proposed dividend of previous year is paid and will be shown as cash outflow of financing activities. Taxation provision of previous year is paid during the current year.
- (5) Non-current assets are disclosed under investing activities. If there is any amount of depreciation or written off it is added back to profit in operating statement.
- (6) Changes in current assets are shown in cash flow statement from operating activities.

**Illustration 8 :** From the following details of Chirag Company compute cash flow from operating activities.

Particulars	(₹)
Profit of current year	3,20,000
Taxation provision	30,000
Proposed dividend	60,000
Goodwill written off	35,000
Depreciation charged	47,000
Loss on sale of asset	43,000
Rent received	45,000
Dividend received	65,000
Increase in current assets	1,00,000
Decrease in current liabilities	90,000

**Ans. :**

**Cash Flow from Operating Activities**

Particulars	(₹)	(₹)
Profit of current year		3,20,000
Add : Non-cash expenses and provisions :		
Taxation provision	30,000	
Proposed dividend	60,000	
Goodwill written off	35,000	
Depreciation charged	47,000	
Loss on sale of asset	43,000	2,15,000
		5,35,000
Less : Non-operating incomes :		
Rent received	45,000	
Dividend received	65,000	1,10,000
<b>Operating profit before changes in working capital</b>		<b>4,25,000</b>
Add : Decrease in current assets	—	
Increase in current liabilities	—	—
		<b>4,25,000</b>
Less : Increase in current assets	1,00,000	
Decrease in current liabilities	90,000	1,90,000
<b>Cash flow from operating activities</b>		<b>2,35,000</b>

**Illustration 9 :** From the following information of Gaurang Company, prepare statement of cash flow from operating activities.

Profit before changes in working capital ₹ 4,95,000; increase in debtors ₹ 75,000; decrease in bills receivables ₹ 40,000; decrease in stock ₹ 30,000; increase in prepaid expenses ₹ 25,000; outstanding expenses (increase) ₹ 15,000; decrease in creditors ₹ 20,000.

**Ans. :**

**Cash Flow from Operating Activities**

Particulars	(₹)	(₹)
Profit before changes in working capital		4,95,000
Add : Decrease in current assets :		
Bills receivable	40,000	
Stock	30,000	
Increase in current liabilities		
Outstanding expenses	15,000	85,000
		<b>5,80,000</b>
Less : Increase in current assets		
Debtors	75,000	
Prepaid expenses	25,000	
Decrease in current liabilities		
Creditors	20,000	1,20,000
<b>Cash flow from operating activities</b>		<b>4,60,000</b>

**Illustration 10 :** From the following details of Mira Limited, prepare cash flow statement of cash flow from operating activities.

**Profit and Loss Statement for the Year Ending on 31-3-2017**

Particulars	(₹)	(₹)
(I) Revenue from sales		28,00,000
(II) Other incomes :		
Income of rent	60,000	
Profit on sale of asset	40,000	
Interest income	90,000	1,90,000
(III) Total income		<b>29,90,000</b>

Particulars	(₹)	(₹)
<b>(IV) Expenses :</b>		
(a) Purchase of goods	21,20,000	
(b) Changes in stock (Opening stock 90,000, Closing stock 1,10,000)	(20,000)	
(c) Employees benefit expenses	1,48,000	
(d) Depreciation on fixed assets	25,000	
(e) Patent amortized	18,000	
(f) Loss on sale of asset	16,000	
(g) Manufacturing expenses	48,000	
(h) Insurance expense	6000	
(i) Salary expense	90,000	
(j) Administrative expense	63,000	
(k) Sales-distribution expenses	7000	25,21,000
<b>(V) Profit before tax</b>		<b>4,69,000</b>

**Information of Current assets and Current liabilities :**

Particulars	Closing balance (31-3-2017)(₹)	Opening balance (31-3-2016)(₹)
Debtors	90,000	78,000
Creditors	80,000	68,000
Bills payables	65,000	75,000
Bills receivables	8000	10,000
Stock	1,10,000	90,000
Outstanding salary	15,000	18,000
Prepaid insurance	7000	9000

**Ans. : Cash Flow from Operating Activities**

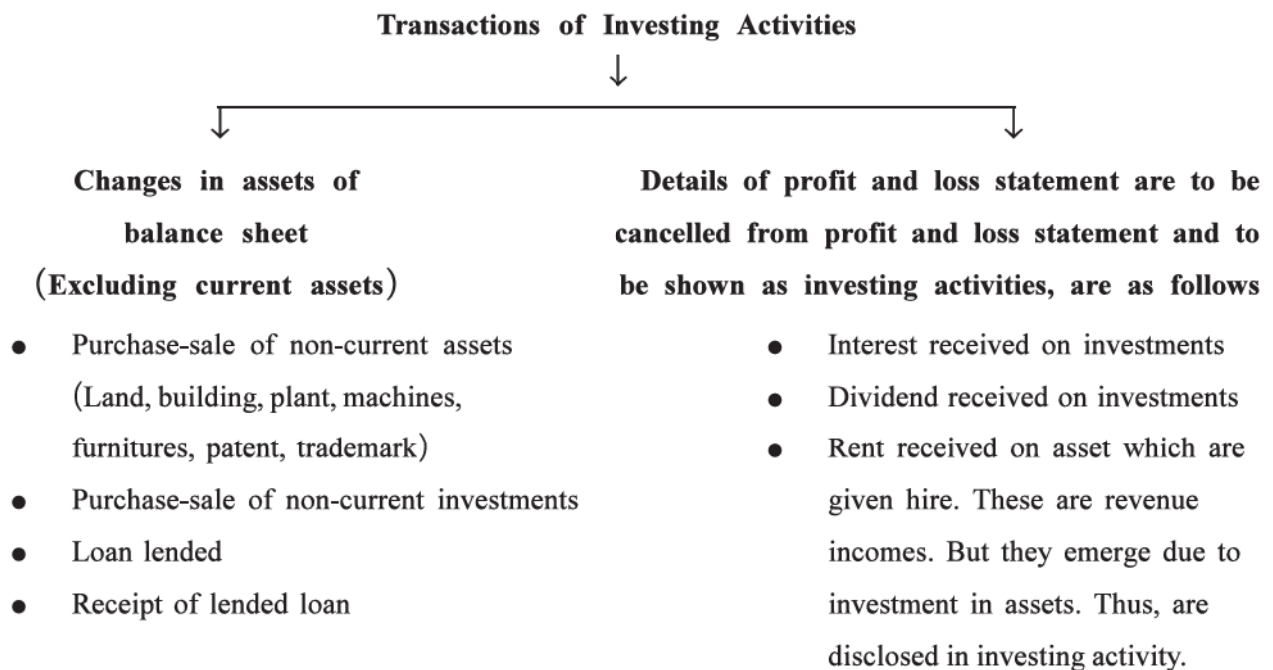
Particulars	(₹)	(₹)
Profit before tax		4,69,000
Add : Non-cash expenses and provisions :		
Depreciation on fixed assets	25,000	
Patent amortized	18,000	
Loss on sale of asset	16,000	59,000
		<b>5,28,000</b>
Less : Non-operating incomes :		
Income of rent	60,000	
Profit on sale of asset	40,000	
Interest income	90,000	1,90,000
<b>Profit before changes in working capital</b>		<b>3,38,000</b>



Particulars	(₹)	(₹)
Add : Decrease in current assets :		
Bills receivable	2000	
Prepaid insurance	2000	
Increase in current liabilities :		
Creditors	12,000	16,000
		<b>3,54,000</b>
Less : Increase in current assets :		
Debtors	12,000	
Stock	20,000	
Decrease in current liabilities :		
Bills payables	10,000	
Salary outstanding	3000	45,000
<b>Cash flow from operating activities</b>		<b>3,09,000</b>

#### 7. Cash Flow From Investing Activities

Transactions of investing activities means changes in details of assets (excluding current assets) side of balance sheet and changes in assets related items. A detailed explanation in this regard is as follows :



Fixed tangible assets are included as a part of non-current assets in investing activities. e.g. plant, machines, furniture (depreciable assets).

- Price of purchased asset is not provided.
- Price of sold asset is not provided.
- Amount of depreciation is not provided.
- Profit of sold asset is not provided.
- Loss of sold asset is not provided.

**Illustration 11 :** From the following information of Nirali Company Ltd. determine cash flow from investing activities.

Particulars	(₹)	Particulars	(₹)
Opening balance of machines	4,50,000	Depreciation provided on machines	50,000
Closing balance of machines	4,00,000	Selling price of machine	15,000
Book value of machine sold during the year	25,000		

### Machine Account

Cr

Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	4,50,000	By Depreciation A/c	50,000
To Cash A/c (?) (Purchase)	25,000	By Cash A/c (Sale)	15,000
		By loss on sale of machine A/c	10,000
		By balance c/d	4,00,000
	<b>4,75,000</b>		<b>4,75,000</b>

Particulars	Amt. (₹)
Sale of machine	15,000
Purchase of machine	(25,000)
Cash outflow from investing activities	(10,000)

- (1) Machine is an asset, thus its balance is debit balance. Therefore its opening balance is shown on debit side.
- (2) Depreciation machine : Journal entry will be as follows :  
Depreciation A/c ...Dr      50,000  

To Machine A/c                          50,000
- (3) Sale of machine : Book value    ₹ 25,000  
Selling price         ₹ 15,000  
Loss                     ₹ 10,000

Cash A/c ...Dr 15,000  
 Loss on sale of machine A/c...Dr 10,000  
     To Machine A/c 25,000

- (4) When machine account is closed, difference is appeared on debit side, it is purchase of new machine :

No.	Activity	Effect
1.	Sale of machine ₹ 15,000 – investing activity	Cash inflow from investing activity
2.	Purchase of machine ₹ 25,000 – investing activity	Cash outflow from investing activity
3.	Depreciation ₹ 50,000 – operating activity	Non-cash transaction, will be added to operating profit
4.	Loss on sale of machine ₹ 10,000	Non-cash transaction, will be added back to operating profit

**Illustration 12 :** From the following details of Mansi Company Ltd., determine and explain transactions influencing operating profit and cash flow from investing activities.

Particulars	(₹)	Particulars	(₹)
Opening balance of furniture	12,00,000	Sale of furniture	4,00,000
Closing balance of furniture	18,00,000	Book value of furniture sold	3,20,000
Depreciation on furniture	2,00,000		

**Ans. :** To find out investing activities, furniture account will be prepared as follows :

**Furniture Account**

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	12,00,000	By Cash A/c (Sale)	4,00,000
To Profit on sale of furniture	80,000	By Depreciation A/c	2,00,000
To Cash A/c (?) (Purchase)	11,20,000	By Balance c/d	18,00,000
	<b>24,00,000</b>		<b>24,00,000</b>

**Statement of Cash Flow From Investing Activities**

Particulars	Amt. (₹)
Sale of furniture	4,00,000
Purchase of furniture	(11,20,000)
Cash flow from investing activities	(7,20,000)

**Explanation :**

- (1) Furniture is an asset, therefore it's opening balance is debit balance.

- |                        |          |          |
|------------------------|----------|----------|
| Depreciation A/c ...Dr | 2,00,000 |          |
| To Furniture A/c       |          | 2,00,000 |

- |                 |            |
|-----------------|------------|
| Book value      | ₹ 3,20,000 |
| – Selling price | ₹ 4,00,000 |
| Profit          | ₹ 80,000   |

- |                                    |        |        |
|------------------------------------|--------|--------|
| (b) Furniture A/c ...Dr            | 80,000 |        |
| To Profit on sale of furniture A/c |        | 80,000 |

- | No. | Activity   | Effect   |
|-----|--|--|
| 1.  | Sale of furniture ₹ 4,00,000 – Investing activity      | Cash inflow from investing activity.                           |
| 2.  | Purchase of furniture ₹ 11,20,000 – Investing activity | Cash outflow from investing activity.                          |
| 3.  | Depreciation ₹ 2,00,000 – Operating activity           | Non-cash transaction will be added to operating profit.        |
| 4.  | Profit on sale of furniture ₹ 80,000                   | Non-cash transaction will be deducted from operating activity. |

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
Investment in 12 % debentures of X Co.	6,00,000	4,00,000
Machines	4,00,000	2,00,000
Land-building	6,00,000	6,00,000
Furniture	1,00,000	80,000
Patent	80,000	1,00,000
Goodwill	60,000	90,000

- (1) Provide 20 % depreciation on machines.
- (2) Provide 10 % depreciation on furniture.
- (3) In the beginning of the year, 40 % investments sold for ₹ 3,00,000.
- (4) Interest received on investments ₹ 60,000.

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### Machine Account

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	2,00,000	By Depreciation A/c, 20 %	40,000
To Cash A/c (Purchase)	2,40,000	By Balance c/d	4,00,000
	4,40,000		4,40,000

### Furniture Account

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	80,000	By Depreciation A/c, 10 %	8000
To Cash A/c (Purchase)	28,000	By Balance c/d	1,00,000
	1,08,000		1,08,000

### Investments Account

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	4,00,000	By Cash A/c	3,00,000
To profit on sale of investment A/c	1,40,000		
To Cash A/c (Purchase)	3,60,000	By Balance c/d	6,00,000
	9,00,000		9,00,000

#### Explanation :

(1) Opening balance of investments ₹ 4,00,000

Sale of 40 % (4,00,000 × 40 %)	₹ 1,60,000
Less : Selling price	₹ 3,00,000
Profit on sale of investments	₹ 1,40,000

(a) Cash A/c ...Dr 3,00,000  
       To Investments A/c 3,00,000

(b) Investments A/c ...Dr 1,40,000  
       To Profit on sale of investments A/c 1,40,000

Sale of investments ₹ 3,00,000 will be shown as cash inflow of investing activity. Profit on sale of investment will be deducted from operating profit.

(2) Depreciation on machine will be calculated on opening balance. Thus 20 % of ₹ 2,00,000 = ₹ 40,000, will be added to operating profit. Debit side difference of ₹ 2,40,000 is appeared, which is purchase of machine, it is shown as cash outflow from investing activity.

- (3) Depreciation on furniture will be calculated on opening balance. Thus 10 % of ₹ 80,000 = ₹ 8000, will be added to operating profit. Debit side difference of ₹ 28,000 is appeared which is purchase of furniture, which is treated as cash outflow from investing activity.
- (4) Interest on investment will be deducted from operating profit and will be shown cash inflow from investing activity.
- (5) Closing balance of patent is ₹ 80,000 and opening balance is ₹ 1,00,000, this shows decrease of ₹ 20,000. This is non-cash transaction, which will be added to operating profit.
- (6) Closing balance of goodwill is ₹ 60,000 and opening balance is ₹ 90,000. This shows decrease of ₹ 30,000. This is non-cash transaction, will be added to operating profit.

#### Statement of Cash Flow from Investing Activities

Particulars	(₹)
Sale of investments	3,00,000
Purchase of machine	(2,40,000)
Purchase of furniture	(28,000)
Interest on investments	60,000
Purchase of investments	(3,60,000)
Cash outflow from investing activities	(2,68,000)

Amounts other than brackets are cash inflow. Amounts shown in brackets are cash outflow.

#### 8. Cash Flow from Financing Activities :

Transactions of financing activities means changes in details of equity and liabilities (excluding current liabilities) side of balance sheet and changes in equity and liabilities related items.

Details included in financing activities are as follows :

#### Transactions of Financing Activities

<p style="text-align: center;">↓</p> <p style="text-align: center;">↓</p> <p><b>Changes in equity and liabilities of balance sheet (Excluding current liabilities)</b></p> <ul style="list-style-type: none"> <li>● Issue of equity and preference share</li> <li>● Buy back of equity shares and redemption of preference share</li> <li>● Issue of new debentures</li> <li>● Redemption of debentures</li> <li>● Borrowing through bank over draft or redemption of bank overdraft</li> <li>● Borrowing through loan or redemption of loan</li> </ul>	<p style="text-align: center;">↓</p> <p style="text-align: center;">↓</p> <p><b>Details of profit and loss statement are to be cancelled from profit and loss statement and to be shown as financing activities are as follows :</b></p> <ul style="list-style-type: none"> <li>● Equity share dividend</li> <li>● Preference share dividend</li> <li>● Interest on debentures or loan</li> </ul> <p>These transactions are expenses and appropriation. But for cash flow statement these are treated as return of capital. Thus, they are disclosed as financing activities.</p>
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● **Special Transactions :**

- (1) The following transactions show changes in size/composition of owners capital and borrowed capital of business entity. Still, these are not considered as cash flow from financing activities.
  - (a) Increase in equity share capital due to issue of bonus share. This transaction shows capitalization of profit or reserve. Capitalization of profit and reserve means conversion of credit balance of profit and loss A/c, general reserve into equity share capital. This transaction gives increase in equity without cash.
  - (b) There is a conversion of debentures into share. In this transaction also, there is no cash movement. Thus, there is no creation of cash flow.
- (2) (a) When issue of equity share and/or debentures is done at premium, the amount of premium is also considered as cash in flow from financing activities.
  - (b) Under writing commission paid at the time of issue of share or debentures is also financing activity and is shown as cash outflow from financing activity.
- (3) Bank overdraft and cash credit, both are short-term borrowings but are treated as financing activities.

**Illustration 14 :** From the following information of Hetal Company Ltd., calculate cash flow from financing activities.

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
Equity share capital	18,00,000	12,00,000
Preference share capital	8,00,000	10,00,000
Debenture	6,00,000	6,00,000

**Additional information :**

- (1) Dividend paid : Equity share capital ₹ 2,00,000, Preference share capital ₹ 1,00,000
- (2) Debenture interest paid ₹ 50,000

**Ans. :**

**Statement of Cash Flow from Financing Activities**

Particulars	(₹)
Equity share capital (Increase in capital)	6,00,000
Redemption of preference share capital (Reduction in share capital)	(2,00,000)
Debenture (No change)	—
Payment of equity share dividend	(2,00,000)
Payment of preference share dividend	(1,00,000)
Payment of debenture interest	(50,000)
Cash flow from financing activities	50,000

● **Stages for preparation of cash flow statement :**

- (1) First of all see adjustments (additional information) and accordingly prepare necessary accounts. As per the syllabus the fixed assets A/c, depreciation fund A/c and taxation provision A/c are included. Give accounting effects to the transactions of these accounts to the operating activities, investing activities or financing activities.

(2) Prepare cash flow statement :

- (a) In the beginning of this statement consider transactions pertaining to cash flow from operating activities. Add back non-cash expenses and provisions to the profit of current year. Deduct non-operating incomes from profit of current year.

After incorporation of accounting effects of these transactions, incorporate effects of changes in working capital. Add reduction in current assets and increase in current liabilities. Deduct increase in current assets and decrease in current liabilities. Deduct tax payment from profit, if any. Difference will be the cash flow from the operating activities.

- (b) Incorporate accounting effect of cash flow transactions of investing activities, where sale of non-current assets will be shown as cash inflow and purchase of non-current assets as cash outflow.

- (c) Finally, incorporate accounting effect of cash flow transactions to financing activities. Increase in share capital or increase in non-current liabilities, will be shown as cash inflow and reduction in share capital and non-current liabilities as cash outflow.

- (d) The total of above stated activities

- Cash flow from operating activities
- Cash flow from investing activities and
- Cash flow from financing activities, will be receipt or payment of cash and cash equivalent.

The addition of opening balance of cash and cash equivalent to this total would give closing balance of cash and cash equivalent.

When the final answer of these activities is identical to cash and cash equivalent to closing balance of cash and cash equivalent it shows possibilities of all correct calculations. The closing balance of cash and cash equivalent in cash flow statement establishes the correctness of answer.

**Illustration 15 :** Following are the balance sheets as at 31-3-2016 and 31-3-2017 of Dahod Company Ltd., prepare cash flow statement.

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
<b>I Equity and Liabilities :</b>		
<b>(1) Shareholders' Funds</b>		
(a) Share capital	20,00,000	18,00,000
(b) Reserves and surplus	7,50,000	5,00,000
<b>(2) Non-current Liabilities</b>		
10 % debentures	5,00,000	7,00,000
<b>(3) Current Liabilities</b>	4,00,000	3,00,000
<b>Total</b>	<b>36,50,000</b>	<b>33,00,000</b>
<b>II Assets :</b>		
<b>(1) Fixed assets</b>		
(i) Tangible assets : Land-building	22,00,000	20,00,000
(ii) Intangible assets : Patent	6,00,000	6,00,000
<b>(2) Current assets : (Excluding cash)</b>	7,00,000	6,00,000
Cash and cash equivalent	1,50,000	1,00,000
<b>Total</b>	<b>36,50,000</b>	<b>33,00,000</b>

**Note :** Debentures are redeemed at the beginning of the year.

**Ans. : Explanation :**

No.	Transaction	Effect
1.	Increase in equity share capital ₹ 2,00,000 (₹ 20,00,000 – ₹ 18,00,000)	Cash inflow of financing activity
2.	Profit of current year ₹ 2,50,000 (₹ 7,50,000 – ₹ 5,00,000)	It will be considered for operating activities
3.	Reduction in 10 % debentures ₹ 2,00,000 (₹ 5,00,000 – ₹ 7,00,000)	Cash outflow of financing activities
4.	Increase in current liabilities ₹ 1,00,000 (₹ 4,00,000 – ₹ 3,00,000)	It will be added to operating activities
5.	Increase in fixed assets (Land-building) ₹ 2,00,000 (₹ 22,00,000 – ₹ 20,00,000)	Cash outflow of investing activities
6.	No change in fixed assets(Patent)	No effect
7.	Increase in current assets ₹ 1,00,000 (₹ 7,00,000 – ₹ 6,00,000)	It will be deducted from operating activities

**Ans. : Cash Flow Statement as at 31-3-2017 of Dahod Company Limited**

Particulars	(₹)	(₹)
(A) Cash flow from operating activities		
Closing balance of P & L A/c (Reserves and surplus)	7,50,000	
Less : Opening balance of P & L A/c (Reserves and surplus)	5,00,000	
Profit for the year		2,50,000
Add : Non-cash expenses (Provisions)		—
Interest on debentures		50,000
Less : Non-operating incomes		—
Operating profit before changes in working capital		3,00,000
Add : Decrease in current assets		—
Increase in current liabilities	1,00,000	1,00,000
		4,00,000
Less : Increase in current assets	1,00,000	1,00,000
Decrease in current liabilities		
(A)		3,00,000
(B) Cash flow from investing activities		
Purchase of land-building	(2,00,000)	(2,00,000)
		1,00,000



Particulars	(₹)	(₹)
(C) Cash flow from financing activities :		
Increase in share capital	2,00,000	
Interest on debentures	(50,000)	
10 % debentures redeemed	(2,00,000)	(50,000)
(D) Increase in cash and cash equivalent (A + B + C)		50,000
Add : Opening balance of cash and cash equivalent		1,00,000
(E) Closing balance of cash and cash equivalent		1,50,000

**Special Note :** To provide comprehensive information of cash flow statement to the students, illustration no. 16 is given, where all three activities are covered. These kind of questions are not expected in exam.

**Illustration 16 :** From the following details of Somnath Company Ltd., prepare cash flow statement as at 31-3-2017.

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
<b>I Equity and Liabilities</b>		
<b>(1) Shareholders' Funds</b>		
(a) Equity share capital	18,00,000	16,00,000
Preference share capital	2,00,000	—
(b) Reserves and surplus : General reserve	1,00,000	80,000
Profit and loss A/c	48,000	40,000
<b>(2) Non-current Liabilities :</b>		
14 % debentures	2,60,000	2,40,000
<b>(3) Current Liabilities :</b>		
Bank overdraft	2,72,000	5,00,000
Trade payables	4,40,000	4,80,000
Short-term provisions :		
Taxation provision	1,68,000	1,20,000
Proposed dividend	2,32,000	2,00,000
<b>Total</b>	<b>35,20,000</b>	<b>32,60,000</b>
<b>II Assets :</b>		
<b>(1) Non-current assets :</b>		
Fixed assets : Tangible	16,00,000	16,40,000
Less : Depreciation fund	6,00,000	4,40,000
	10,00,000	12,00,000
<b>(2) Current assets :</b>		
Trade payables	9,60,000	8,00,000
Stock	14,00,000	12,00,000
Cash and cash equivalent	1,60,000	60,000
<b>Total</b>	<b>35,20,000</b>	<b>32,60,000</b>

**Additional information :**

- (1) Interest paid on debentures ₹ 36,000  
 (2) Taxes paid ₹ 1,68,000

**Ans. : Explanation :**

No.	Transactions	Effects
1.	Increase in equity share capital ₹ 2,00,000 (₹ 18,00,000 – ₹ 16,00,000)	Cash inflow of financing activity shown as cash inflow
2.	Increase in preference share capital ₹ 2,00,000 (₹ 2,00,000 – Zero)	Cash inflow of financing activity
3.	Increase in general reserve ₹ 20,000 (₹ 1,00,000 – ₹ 80,000)	It will be added to profit in operating statement under the head of provision
4.	Profit and loss A/c. Profit of current year ₹ 8000 (₹ 48,000 – ₹ 40,000)	It will be considered as operating activities
5.	Increase in 14 % debentures ₹ 20,000 (₹ 2,60,000 – ₹ 2,40,000)	Cash inflow of financing activities
6.	Current liabilities : – Decrease in bank overdraft ₹ 2,28,000 (₹ 2,72,000 – ₹ 5,00,000) – Decrease in trade payables ₹ 40,000 (₹ 4,40,000 – ₹ 4,80,000) – Taxation provision  – Proposed dividend	Cash outflow of financing activities  It will be deducted in operating statement  In adjustment payment is given, so account will be opened and accordingly treatments will be given. Proposed dividend of last year will be shown as cash outflow of financing activities. Proposed dividend of current year will be added to net profit under cash flow from operating activities.
7.	Fixed assets (tangible) and Depreciation	Fixed assets A/c and depreciation A/c will be opened and treatments will be given accordingly
8.	Current assets : – Increase in trade receivables ₹ 1,60,000 (₹ 9,60,000 – ₹ 8,00,000) – Increase in stock ₹ 2,00,000 (₹ 16,00,000 – ₹ 14,00,000)	It will be deducted from operating cash flow statement It will be deducted from operating cash flow statement
9.	Debenture interest paid ₹ 36,000	It will be added back to profit in operating statement and will be shown as cash outflow of financing activity

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Cash A/c (Payment) (will be deducted from operating activity)	1,68,000	By Balance b/d	1,20,000
To Balance c/d	1,68,000	By P & L A/c (Provision) (Will be added to operating activity)	2,16,000
	<b>3,36,000</b>		<b>3,36,000</b>

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	16,40,000	By Cash A/c (Sale) (Cash inflow from investing activity)	40,000
		By Balance c/d	16,00,000
	<b>16,40,000</b>		<b>16,40,000</b>

Dr		Cr	
Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance c/d		By Balance b/d	4,40,000
	6,00,000	By Profit and Loss A/c (Provision)	1,60,000
	<b>6,00,000</b>		<b>6,00,000</b>

- Tax :

Depreciation and fixed assets :

(1) Profit and loss ...Dr	1,60,000	
To Depreciation fund A/c		1,60,000
(2) Fixed assets A/c ...Dr	1,20,000	
To Cash A/c		1,20,000

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**Cash Flow Statement as at 31-3-2017 of Somnath Limited**

Particulars	(₹)	(₹)
(A) Cash flow from operating activities :		
Closing balance of profit and loss A/c	48,000	
Less : Opening balance of profit and loss A/c	40,000	
Profit of current year		8000
Add : Non-cash expenses (Provisions)		
Taxation provision	2,16,000	
Depreciation	1,60,000	
General reserve	20,000	
Proposed dividend	2,32,000	
Debenture Interest	36,000	6,64,000
		6,72,000
	—	—
Less : Non-operating income		6,72,000
Profit before changes in working capital		—
Add : Decrease in current assets		—
Increase in current liabilities		—
		6,72,000
Less : Increase in current assets		
Increase in trade receivables	1,60,000	
Increase in stock	2,00,000	
Decrease in current liabilities :		
Trade payables	40,000	4,00,000
		2,72,000
Less : Tax paid		1,68,000
		1,04,000
(B) Cash flow from investing activities :		
Sale of fixed assets	40,000	40,000
(C) Cash flow from financing activities :		1,44,000
Increase in equity share capital	2,00,000	
Increase in preference share capital	2,00,000	
Issued 14 % debentures	20,000	
Redemption of bank overdraft	(2,28,000)	
Proposed dividend	(2,00,000)	
Debenture interest paid	(36,000)	(44,000)
(D) Cash and cash equivalent		1,00,000
Add : Opening balance of cash and cash equivalent		60,000
Closing balance of cash and cash equivalent		1,60,000

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### Exercise

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**1. Select appropriate option for every question :**

- (1) How many activities are there in cash flow statement ?  
(a) Five (b) Four  
(c) Three (d) Two
- (2) Cash equivalent has ..... .  
(a) higher liquidity (b) higher solvency  
(c) higher profitability (d) all of the above
- (3) Decrease in current assets and increase in current liabilities ..... .  
(a) are cash inflow and cash outflow respectively  
(b) are cash outflow and cash inflow respectively  
(c) both are cash inflows  
(d) both are cash outflows
- (4) Increased in current assets and decrease in current liabilities ..... .  
(a) both are cash outflows  
(b) both are cash inflows  
(c) are cash outflow and cash inflow respectively  
(d) are cash inflow and cash outflow respectively
- (5) Collection of debtors and bills receivable is ..... .  
(a) cash inflow of operating activity  
(b) cash outflow of operating activity  
(c) cash inflow of financing activity  
(d) cash inflow of investing activity
- (6) Which of the following transaction is always transaction of operating activity ?  
(a) Interest paid on loan (b) Dividend received  
(c) Dividend paid (d) Salary expense
- (7) Dividend or interest received on investment is ..... .  
(a) added to cash flow of operating activity  
(b) deducted from cash flow of financing activity  
(c) added to cash flow of investing activity  
(d) deducted from cash flow of investing activity
- (8) Bank overdraft ..... .  
(a) is current liability but considered as financing activity  
(b) is current liability but considered as operating activity  
(c) is current liability but considered as investing activity  
(d) is not activity of cash flow statement
- (9) Rent received ..... .  
(a) is added to operating activity and deducted from financing activity  
(b) is added to operating activity and added to financing activity  
(c) is added to operating activity and added to investing activity  
(d) is deducted from operating activity and added to investing activity



- (10) Reduction in goodwill in current year as compared to previous year is ..... .  
 (a) sale of goodwill (b) purchase of goodwill  
 (c) written off goodwill (d) all of the above
- (11) Cash deposited in bank is ..... .  
 (a) cash outflow of operating activity  
 (b) cash outflow of financing activity  
 (c) cash outflow of investing activity  
 (d) not cash flow
- (12) Which of the following is included in financial expense ?  
 (a) Factory expenses (b) Administrative expenses  
 (c) Sales expenses (d) Interest expenses
- (13) Payment of interim dividend is ..... .  
 (a) deducted from operating statement and added to financing activity  
 (b) deducted from operating statement and added to investing activity  
 (c) added to operating statement and deducted from financing activity  
 (d) none of the above

**2. Answer the following in one sentence :**

- (1) What is cash flow ?
- (2) What is cash and cash equivalent ?
- (3) What is cash flow statement ?
- (4) What is operating activities ?
- (5) What is investing activities ?
- (6) What is financing activities ?
- (7) Which transactions are always operating activities ?
- (8) Which transactions are always investing activities ?
- (9) Which transactions are always financing activities ?
- (10) Give illustration of such transaction from where two activities are taking place.
- (11) Give illustration of is cash transaction but not cash flow'.
- (12) Where are the self constructed assets recorded ?
- (13) To which activity increase/decrease of bank overdraft is recorded ?
- (14) For which activity underwriting commission paid is considered ?
- (15) As which activity income tax payment and income tax refund are considered ? Why ?
- (16) Give illustration of any two operating incomes.
- (17) Where addition in general reserve is recorded ?
- (18) Describe whether cash flow would increase or decrease due to following transactions ?  
 (i) Increase in current assets (ii) Decrease in current assets  
 (iii) Increase in current liabilities (iv) Decrease in current liabilities
- (19) In which activity the received dividend and interest are recorded ?
- (20) In which activity the paid dividend and interest are recorded ?

**3. Answer the following questions in brief :**

- (1) Describe the operating activities for the following companies :  
 (i) Trading companies (ii) Insurance companies (iii) Bank

- (2) Explain cash flow from operating transactions of non-finance companies and finance companies.
- (3) From the following transactions, identify transactions of operating activities :
- |                           |   |
|---------------------------|---|
| (i) Wages paid            | (vii) Paid office expenses              |
| (ii) Purchase of building | (viii) Paid sales-distribution expenses |
| (iii) Sale of furniture   | (ix) Carriage inward                    |
| (iv) Payment to creditors | (x) Carriage outward                    |
| (v) Dividend paid         | (xi) Royalty paid                       |
| (vi) Rent paid            | (xii) Income tax paid                   |
4. Explain cash flow transactions of investing activities.
5. From the following transactions, identify transactions of investing activities :
- |                                       |  |
|---------------------------------------|--|
| (i) Salary paid                       | (vii) Sale of furniture                |
| (ii) Rent paid                        | (viii) Collection from debtors         |
| (iii) Purchase of investments         | (ix) Payment to creditors              |
| (iv) Sale of land                     | (x) Issue of equity shares             |
| (v) Purchase of building              | (xi) Redemption of debentures          |
| (vi) Interest received on investments | (xii) Dividend received on investments |
6. Explain – Cash flow transactions of financing activities.
7. From the following transactions, identify transactions of financing activities :
- |   |                                |
|---|--------------------------------|
| (i) Sale of machine                         | (vii) Purchase of investments  |
| (ii) Redemption of preference share capital | (viii) Issue new equity shares |
| (iii) Dividend paid                         | (ix) Paid interim dividend     |
| (iv) Interest paid                          | (x) Interest received          |
| (v) Dividend received                       | (xi) Borrowed bank loan        |
| (vi) Borrowed bank overdraft                | (xii) Commission received      |
8. What are non-cash transactions ? Give two illustrations.
9. What are non-operating incomes ? Give two illustrations.
10. Where interim dividend is recorded in cash flow statement ?
11. Where accounting treatments of taxation provision and tax payment are given in cash flow statement ?
12. Explain effect of bonus share in cash flow statement.
13. Where conversion of debentures into share is recorded in cash flow statement ?
14. Which kind of activity is the payment of underwriting commission ? Why ?
15. From the following transactions calculate cash flow from operating activities :

Particulars	(₹)
Profit before taxes	99,000
Income tax provision	29,000
Proposed dividend	39,000
Depreciation	22,000
Dividend received	21,000
Interest received	20,000
Interest paid	28,000
Goodwill written off	15,000
Profit on sale of asset	12,000

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

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
Profit and loss A/c	45,000	30,000
Depreciation	90,000	70,000
Goodwill	40,000	55,000
Stock	60,000	45,000
Debtors	50,000	90,000
Creditors	40,000	60,000
Bills payables	70,000	20,000
Prepaid expenses	10,000	15,000

**Additional information :**

- (i) Dividend received ₹ 2000
- (ii) Interest paid ₹ 3000
- (iii) Rent received ₹ 10,000

17. From the following information calculate cash flow from operating activities :

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
Profit and loss A/c	60,000	25,000
General reserve	45,000	35,000
Taxation provision	38,000	48,000
Depreciation fund	42,000	32,000
Goodwill	27,000	38,000
Debtors	49,000	39,000
Creditors	39,000	29,000
Outstanding expenses	12,000	17,000
Prepaid expenses	14,000	10,000

**Additional information :**

- (i) Profit on sale of assets ₹ 15,000
- (ii) Loss on sale of furniture ₹ 8000
- (iii) Income of rent ₹ 48,000
- (iv) Interest paid on debentures ₹ 32,000
- (v) Dividend payment ₹ 10,000

18. From the following given information calculate cash flow from investing activities :

Particulars	(₹)
Sale of non-current investments	88,000
Purchase of land	1,48,000
Purchase of machine	98,000
Sale of furniture	45,000
Dividend received on investments	40,000
Paid for goodwill	32,000
Issue of shares	1,20,000
Redemption of debentures	45,000
Loan borrowed	28,000

19. From the following given details calculate cash flow from investing activities :

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
Plant and machines	9,20,000	7,20,000
Depreciation fund on plant and machines	1,50,000	1,20,000
Goodwill	90,000	95,000
Patent	70,000	1,30,000
10 % investments	95,000	2,70,000
General reserve	45,000	30,000
Profit and loss A/c	60,000	40,000
Equity share capital	6,00,000	4,50,000
Bank loan	1,00,000	1,50,000
Current liabilities	90,000	60,000
Interest received on investments ₹ 18,000		
Some of the patents were sold during the year.		

20. From the following information calculate cash flow from financing activities :

Particulars	(₹)
Purchase of land	1,88,000
Equity shares issued	1,45,000
Redemption of preference shares	60,000
Redemption of debentures	70,000
Borrowed bank loan	90,000
Debenture interest paid	6000
Dividend paid	8000
Dividend-interest received	9000
Sale of furniture	32,000
Purchase of machine	68,000
Interest received on investments	13,000
Paid for patents	19,000

21. From the following information calculate cash flow from financing activities :

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
10 % debentures	2,45,000	1,95,000
Equity share capital	3,45,000	2,50,000
12 % debentures	1,00,000	1,50,000
Preference share capital	80,000	1,00,000
Bank overdraft	45,000	68,000

**Additional information :**

- (1) Debenture interest paid ₹ 12,000
- (2) Paid ₹ 22,000 for equity share dividend and preference share dividend
- (3) Paid bank overdraft ₹ 4000

