



Accounting Standard (AS) - 3 Cash Flow Statements

Introduction

- ▶ Cash flow statement is additional information to user of financial statement
- ▶ This statement exhibits the flow of incoming and outgoing cash
- ▶ This statement assesses the ability of the enterprise to generate cash and cash equivalents
- ▶ It also assesses the needs of the enterprise to utilise the cash and cash equivalents generated
- ▶ It also assesses the liquidity and solvency of the enterprise.

Applicability

- ▶ This standard applies to the enterprises:
 - ▶ Having turnover more than Rs. 50 Crores in a financial year; or Entities having borrowings more than Rs. 10 Crores at any time during the Immediately preceding accounting period.
 - ▶ Listed companies;
 - ▶ Cash flow statement of listed companies shall be presented only under the indirect method as prescribed in AS 3

Definitions

- ▶ **Cash comprises cash on hand and demand deposits with banks.**
- ▶ **Cash equivalents are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.**
- ▶ **Cash flows are inflows and outflows of cash and cash equivalents.**
- ▶ **Operating activities are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities.**
- ▶ **Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.**
- ▶ **Financing activities are activities that result in changes in the size and composition of the owners' capital (including preference share capital in the case of a company) and borrowings of the enterprise.**

Cash and Cash Equivalents

- Cash Equivalents
 - Held for meeting short term commitments
 - It is readily convertible into known amounts of cash
 - It has a very insignificant risk
 - Short maturity (say 3 months maximum)
- Cash flows exclude
 - Movements between cash and cash equivalents
- Cash management includes the investment of excess cash in cash equivalents

Features of Cash Flow Statement

- ▶ *The cash flow statement should report cash flows during the period classified by*
 - ▶ *Operating,*
 - ▶ *Investing and*
 - ▶ *Financing activities.*

- ▶ Sum of these three types of cash flow reflect net increase or decrease of cash and cash equivalents.

Operating Activities

- ▶ These are principal revenue producing activities of the enterprise.
- ▶ Examples:
 - ▶ Cash receipts from sale of goods / rendering services;
 - ▶ Cash receipts from royalties, fees, commissions and other revenue;
 - ▶ Cash payments to suppliers of goods and service;
 - ▶ Cash payments to and on behalf of employees.

Investment Activities

- ▶ The activities of acquisition and disposal of long term assets and other investments not included in cash equivalent are investing activities.
- ▶ It includes making and collecting loans, acquiring and disposal of debt and equity instruments, property and fixed assets etc.
- ▶ Examples of cash flows arising from investing activities are as follows:
 - ▶ Cash payments to acquire fixed assets
 - ▶ Cash receipts from disposal of fixed assets
 - ▶ Cash payments to acquire shares, warrants or debt instruments of other enterprises and interest in joint ventures
 - ▶ Cash receipt from disposal of above investments

Financing Activities

- Those activities that result in changes in size and composition of owners capital and borrowing of the organization.
- It includes receipts from issuing shares, debentures, bonds, borrowing and payment of borrowed amount, loan etc.
 - Sale of share
 - Buy back of shares
 - Redemption of preference shares
 - Issue / redemption of debentures
 - Long term loan / payment thereof
 - Dividend / interest paid

Cash flow from operating activities

- ▶ It can be derived either from direct method or indirect method
 - ▶ Direct method:
 - ▶ In this method, gross receipts and gross payments of cash are disclosed
 - ▶ Indirect method:
 - ▶ In this method, profit and loss account is adjusted for the effects of transaction of non-cash nature.

Interest

▶ Interest Received

- ▶ Received from investment - it is in investment activities
- ▶ Received from short term investment classified, as cash equivalents should be considered as cash inflows from operating activities.
- ▶ Received on trade advances and operating receivables should be in operating activities

▶ Interest Paid

- ▶ On loans / debts are in financing activities
 - ▶ On working capital loan and any other loan taken to finance operating activities are in operating activities
- ▶ Cash flow from interest should be separately disclosed.

Dividend

- Dividend Received
 - For financial enterprises - in operating activities
 - For other than financial enterprises - in investing activities
- Dividend Paid
 - Always classified as financing activities
- Cash flow from dividend should be separately disclosed

Foreign currency transaction

- ▶ The effect of change in exchange rate in cash and cash equivalents held in foreign currency should be reported as separate part of the reconciliation of cash and cash equivalents.
- ▶ Unrealized gain and losses arising from changes in foreign exchanges rates are not cash flows.

Example

- ▶ Z Ltd. Has no foreign currency cash flow for the year 2009. It holds some deposits in a bank in USA. The balance as on 31/03/2011 and 31/03/2012 were US \$100000 and US\$ 102000 respectively and the respective exchange rates were US \$1= 45, 50. The increase in the balance was on account of Interest credited on 31/12/2012. Thus the deposit was reported at Rs. 45000000 in the Balance sheet as on 31/03/2011 and Rs. 5100000 on 31/12/2012.

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- ▶ The P&L A/c was credited by Rs. 100000(US \$ 2000*Rs. 50) towards interest and by Rs. 500000(100000*(50-45)) due to Exchange difference.
- ▶ In preparing the Cash flow statement Rs. 500000 should be deducted from Net profit before Taxes and extra ordinary items.
- ▶ However in order to reconcile the opening balance of Cash and Cash equivalents with its Closing Balance, the Exchange difference Rs. 500000/- should be added to opening balance in note to Cash Flow statement

Extraordinary items

- ▶ The cash flows associated with extraordinary items should be classified as arising from:
 - ▶ Operating
 - ▶ Investing or
 - ▶ Financing activitiesas appropriate and separately disclosed.

Treatment of tax

- ▶ Cash flow for tax payments / refund should be classified as cash flow from operating activities.
- ▶ If cash flow can be specifically identified as cash flow from investment / financing activities, appropriate classification should be made.

Acquisitions and disposals of subsidiaries and other business units

- Cash flow on acquisition and disposal of subsidiaries and other business units should be :
 - Presented separately
 - Classified as investing activities
 - Total purchase and disposal should be disclosed separately
 - The position of the purchase / disposal consideration discharged by means of cash and cash equivalents should be disclosed

Non-cash transactions

- ▶ These should be excluded from the cash flow statement
- ▶ These transactions should be disclosed in the financial statements.
- ▶ Examples
 - ▶ Acquisition of assets by assuming directly related liabilities
 - ▶ Acquisition of an enterprise by means of issue of equity shares
 - ▶ Conversion of debt to equity

Disclosures of cash and cash equivalents

- ▶ The components of cash and cash equivalents should be disclosed
- ▶ Reconciliation of the amount in the cash flow statement with the equivalent items reported in the balance sheet
- ▶ The amount of cash and cash equivalent balance held by the enterprises that are not available for use by it with explanation of management.

Direct Method Cash Flow Statement

▶ A. CASH FLOWS FROM OPERATING ACTIVITIES

Cash receipts from Customer

(-) Cash paid to suppliers and employees

Cash generated from operations

(-) Income Tax paid

Cash Flow before Extraordinary Items

(+/-) Extraordinary items

NET CASH FROM OPERATING ACTIVITIES

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- ▶ B. Cash flows from investing activities

Proceeds of sale of assets

(-)Purchase of assets

(+) Interest received

(+) Dividend received

NET CASH FROM INVESTING ACTIVITIES

- - ▶ C. Cash flows from Financing activities
 - Proceeds from issue of Share capital
 - (+) Proceeds from long term borrowings
 - (-) Repayment of shares and long term borrowings
 - (-) Interest paid
 - (-) Dividend paid
- CASH FLOW FROM FINANCING
ACTIVITIES**



▶ **NET INCREASE IN CASH & CASH EQUIVALENTS (A+B+C)**

(+) Cash and Cash equivalents at beginning of the period

CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD

INDIRECT METHOD CASH FLOW STATEMENT

▶ A. Cash flows from Operating activities

Net profit before taxation and extraordinary items

Adjustment for:

- (+) Depreciation
- (+) Foreign Exchange loss
- (-) Interest income
- (-) Dividend income

Operating profit before working capital changes

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- ▶ (-) Increase in sundry debtors
- (-) Increase in Inventories
- (+) Increase in sundry creditors
- Cash generated from Operations
- (-) Income Tax paid
- Cash flow before extraordinary items
- (+/-) Extraordinary items
- Cash flow from operating activities

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- B) Cash flow from Investing activities
(SAME AS ABOVE)
- C) Cash flow from Financing Activities
(SAME AS ABOVE)
- NET INCREASE IN CASH & CASH EQUIVALENTS
(A+B+C)
- (+) Cash and Cash equivalents at beginning of the period
- CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD