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CHAPTER

IND AS 7 – STATEMENT OF CASH FLOW

1. Introduction

Statement of Cash Flow (SCF) is an additional information provided to the users of accounts in the form of a statement, which reflects various sources from where cash was generated (inflow of cash) by an entity during the relevant accounting year and how these inflows were utilised (outflow of cash) by the entity. This information is very useful to the users to evaluate the ability of an entity to generate cash and cash equivalents and the timing and certainty of their generation.

2. Objective and benefits of Cash Flow

Statement of cash flow helps the users to assess the entity's

- Ability to generate cash & cash equivalents;
- Utilisation of the cash flows;
- Further requirement of generating cash and cash equivalents;
- Timing, nature and certainty of generation of future cash flows and to check the past assessment accuracy; and
- The changes in the capital structure.

3. Scope

An entity shall prepare a statement of cash flows in accordance with the requirements of this Standard and shall **present it as an integral part** of its financial statements for each period for which financial statements are presented.

4. Definitions

Cash: Cash includes cash in hand, cash at bank **&** demand deposits with banks;

Demand deposits mean deposits which can be withdrawn without prior notice and penalty charges. Generally long term deposits are placed for a specific period in banks and these cannot be withdrawn without penalty, hence it cannot be classified as cash.

Cash equivalents: An asset can be called as a cash equivalent when it satisfies the following conditions:–

1. Short term & highly liquid investments which are readily convertible into cash; and
2. Conversion into cash is subject to ***insignificant risk of changes in value***; (*i.e.*, Insignificant loss because of conversion)

Short term investment is an investment which has a maturity of **less than or equal to three months** from the **date of acquisition**.

E.g.,

- Treasury bills, Government securities having maturity within 3 months from the date of acquisition (These items are redeemed at the same amount without any default – insignificant risk of change in value).
- Preference shares acquired also can be cash equivalent only when the entity acquired 3 months before their specified redemption date and subject to insignificant risk of failure of the company to repay the amount at maturity.
- Investment in equity shares cannot be cash equivalent as it has significant risk of change in value;

An entity should disclose the list of cash and cash equivalents (CE). If the amounts disclosed **as** cash equivalents do NOT match directly with the items in the financial statements, the entity should prepare reconciliation for the same. (Any change in list of Cash and CE - considered as change in accounting policy as per AS 5)

Concept capsule 1

Can '**bank overdraft**' be treated as Cash and Cash equivalents?

Suggested answer

Bank borrowings are generally considered to be financing activities. However, in some countries, bank overdrafts which are **repayable on demand** form an integral part of an entity's cash management. In these circumstances, bank overdrafts are included as a component of cash and cash equivalents. A characteristic of such banking arrangements is that the bank balance often fluctuates from being positive to overdrawn (negative).

Cash credit is a short-term loan. The movement in this cash credit will be considered as financing activities;

Concept capsule 2

Company has provided the following information regarding the various assets held by company on 31st March 20X1. Find out, which of the following items will be part of cash and cash equivalents for the purpose of preparation of cash flow statement as per the guidance provided in Ind AS 7:

Sr. No.	*Name of the Security*	*Additional Information*
1.	*Fixed deposit with SBI*	*12%, 3 years maturity on 1st January 20X4*
2.	*Fixed deposit with HDFC*	*10%, original term was for 2 years, but due for maturity on 30th June 20X1*
3.	*Redeemable Preference shares in ABC Ltd*	*Acquired on 31st January 20X1 and the redemption is due on 30th April 20X1*
4.	*Cash balances at various banks*	*All branches of all banks in India*
5.	*Cash balances at various banks*	*All international branches of Indian banks*
6.	*Cash balances at various banks*	*Branches of foreign banks outside India*
7.	*Bank overdraft of SBI Fort branch*	*Temporary overdraft, which is payable on demand*
8.	*Treasury Bills*	*90 days maturity*

Suggested answer

As per Ind AS 7, Cash equivalent are short term & highly liquid assets which are readily convertible into cash; and conversion into cash is subject to insignificant risk of changes in value; (*i.e.*, Insignificant loss because of conversion)

Sr. No.	Name of the Security	Decision
1.	Fixed deposit with SBI	Not to be considered – long term
2.	Fixed deposit with HDFC	Exclude as original maturity is not less than 90 days from the date of acquisition
3.	Redeemable Preference shares in ABC Ltd.	Include as due within 90 days from the date of acquisition
4.	Cash balances at various banks	Include
5.	Cash balances at various banks	Include
6.	Cash balances at various banks	Include
7.	Bank overdraft of SBI Fort branch	Include (Assumed as integral part of an entity's cash management)
8.	Treasury Bills	Include

Note:

As per Division II Schedule III of the Companies Act, 2013, cash and cash equivalents classification is like this

Cash and Bank Balances

(*i*) Cash and cash equivalents shall be classified as:

(*a*) Balances with banks (of the nature of cash and cash equivalents);

(*b*) Cheques, drafts on hand;

(*c*) Cash on hand;

(*d*) Others (specify nature).

(*ii*) Bank balances **other than** cash and cash equivalents **as above, shall be disclosed below cash and cash equivalents on the face of the Balance Sheet.**

As per the Guidance note –

1. "The disclosure regarding 'bank balances other than cash and cash equivalents' should **include** items such as Balances with banks held as margin money or security against borrowings, guarantees, etc. and bank deposits **with original maturity of more than three months but less than 12 months**".
2. Bank deposits **with more than 12 months maturity** should be classified under **"Other current Financial Assets"** *(read carefully) i.e.,* This presentation only when ***"Original term is more than 12 months but the remaining maturity is less than 12 months from the balance sheet date"*** ;
3. If the Original maturity and **remaining** maturity from the balance sheet date is more than 12 months – it should be presented under **"Other non-current financial assets"**.

Presentation of Statement of Cash Flow (SCF)

As per the standard, CASH ACTIVITIES of an entity are classified into **three**. Such classification should be most appropriate to its business. The classification is based on the nature of business of the entity.

Cash Activities

Operating Activities	Investing Activities	Financing Activities
These are 1. Principal revenue producing activities; **&** 2. Activities which CANNOT be classified as investing or financing activities. It means residuary activities are also operating activities.	1. Purchase **&** sale of long term assets and other Investments which are not cash equivalents; **&** 2. Income received from investments;	1. The activities which changes the size and composition of contributed equity (*i.e.* owners's capital); 2. Borrowings and repayment of borrowings; 3. Financing costs – on equity, preference and borrowings and any other kind of finance;
Examples ◆ Cash received from the sale of goods **or** services; ◆ Payments made to suppliers for goods or services; ◆ Receipt of royalties, fees, commission and other revenue; ◆ Payments to employees; ◆ Payments for other operating expenses; ◆ Insurance premium payments & claims receipts; ◆ Cash theft; (residuary item) ◆ Cash received from insurance claim on fire accident; (residuary item)	◆ Acquisition & disposal of fixed assets including intangibles; ◆ Acquisition & disposal of shares, share warrants, debt securities of other entities; ◆ Loans and advances given to third parties; (Not by Financial entity) ◆ Interest, dividend and rental income receipts; *(Income from investments)*	◆ Issue of equity & preference share capital; ◆ Buy back of equity shares; ◆ Redemption of preference shares; ◆ Borrowing loans & issue of debentures; ◆ Repayment of loans & redemption of debentures; ◆ Interest payment, Preference dividend payment, Equity dividend payment (either interim or final dividend); *(finance costs)* ◆ Cash payments by a lessee for the reduction of the outstanding liability relating to a **lease as per** Ind AS 116.

Broadly SCF is presented in the following manner. It is discussed in detail in the next paragraphs.

Statement of cash flow of X Ltd. for the year ended 31-3-20XX	
Particulars	₹
Cash flows from OPERATING activities	XXX
Cash flows from INVESTING activities	XXX
Cash flows from FINANCING activities	XXX
Net cash flows	XXX
Add: Opening Cash and cash equivalents	XXX
Closing Cash and cash equivalents	XXX

How does the presentation of SCF help the users of financial statements?

It helps the users in many ways while taking economic decisions. Benefits of classification from each activity are described as follows:

- **Operating activities** - To forecast future cash flows from its regular operations;
- **Investment activities**: Helps the users to estimate the future operating cash flows because of the current year investing activities and other income from the investment activities;
- **Financing activities:** It is useful to predict future claims by providers of funds by way of dividend, interest, etc.

Concept capsule 3

During the year Harsha Ltd. acquired 60% equity shares in Y Ltd. for ₹ 50 crore and it **sold** 53% shares in Z Ltd. for ₹ 40 crore. The accountant of the company wants to net off the transactions and disclose ₹ 10 crore (₹ 50 – 40) under investment activities. Comment.

Suggested answer

As per Ind AS 7, acquisitions and disposal of subsidiaries or other business units should NOT be netted off and it requires separate presentation in SCF under investing activities. Hence it should present the transactions in the following manner:–

Investment activities:	₹ (Crores)
Acquisition of subsidiary (Y Ltd.)	(50)
Disposal of subsidiary (Z Ltd.)	40

Concept capsule 4

Manasa Ltd. acquired a car for ₹ 10 lakh on credit of 3 months. Delay in payment is charged with 12% interest. The company paid a total amount of ₹ 10.5 lakh. How should the company present the same in SCF?

Suggested answer

As per Ind AS 7, if a single transaction includes multiple activities – the entity should bifurcate and classify under the respective heads separately based on its nature.

In the given case, payment includes two activities *i.e.*, 1. Payment for the asset (₹ 10 lakh); & 2. Payment of Interest (₹ 0.5 lakh). Payment for the asset is an investment activity and payment of interest is a financing activity. Hence the company should present under the respective activities of SCF.

Concept capsule 5

Laxman Ltd. is into cars **trading *and* renting cabs** business. Some of the cars, which are used for renting, are held for sale at the year end. How to classify subsequent cash flows from sale of such assets?

Suggested answer

Before answering the question directly, we need to recall Ind AS 16 – PPE. As per Ind AS 16, if an entity in the course of its ordinary activities, routinely sells items of PPE that it has held for rental to others shall transfer such assets to inventories at their carrying amount when they cease to be rented and become held for sale. The proceeds from the sale of such assets shall be recognised as revenue in accordance with Ind AS 115 - *Revenue from Contracts with Customers*.

Ind AS 105 does **not apply** when assets that are held for sale in the ordinary course of business are transferred to inventories.

As the assets are classified as inventory and receipts on sale of items are transferred to revenue, it should be classified as operating activities.

Concept capsule 6

(Requires knowledge of Ind AS 109)

An entity has entered into a factoring arrangement and received money from the factor. Examine the said transaction and state how should it be presented in the statement of cash flows?

Suggested answer

Under factoring arrangement, it needs to be assessed whether the arrangement is recourse or non-recourse.

Recourse factoring

In this case, as the company has significant risks and rewards with debtors- the entity does not de-recognise the debtors but the amount received from the factor is recognised as a financial liability. Hence, the amount received will be classified as a **financing cash inflows.**

Subsequently, when the cash is collected by the factor from the customer, the entity de-recognises the liability and the receivables. This amounts to non-cash transaction.

Non-recourse factoring:

Where an entity de-recognises the factored receivables and receives cash from the factor, the cash receipt is classified as an **operating cash inflow**. This is because the entity has received cash in exchange for receivables that arose from its operating activities.

When a contract is accounted for as a hedge of an identifiable position the cash flows of the contract are classified in the same manner as the cash flows of the position being hedged. (*You understand this after studying Ind AS 109 – Financial instruments*)

5. Presentation of cash flows from OPERATING activities

Operating activities can be presented in TWO ways. They are:

1. Direct method;
2. Indirect method.

The standard gives an option to the entity in presentation of operating activities i.e., it can present either in direct method or indirect method. The standard **encourages direct method**.

(1) Direct Method

Under the direct method, the entity gives information about major classes of

- Gross cash receipts; and
- Gross cash payments.

Gross cash receipts or payments of the entity can be obtained from either:

(*a*) Cash/bank book; or

(*b*) Alternatively non-cash and non operating items (*i.e.*, investing or financing items) can be eliminated from P&L statement;

See the format of cash flows from operating activities under direct method:

Cash flows from operating activities	₹
Cash receipts from customers	XXX
Cash paid to suppliers and employees	(XX)
Cash generated from operations	**XXX**
Income tax paid	(XX)

Cash flows from operating activities	₹
Cash flows before extraordinary item	**XXX**
Proceeds from earthquake disaster settlement	XX
Net cash from operating activities	**XXX**

(2) Indirect Method

Under this method, the net cash flows from operating activities are determined by adjusting (add/less) profit or loss **before tax** and **before extraordinary/exceptional** items with:

(*a*) Non-cash items such as depreciation, provisions, goodwill written off, etc.;

(*b*) Non-operating items i.e., investing or financing items which are considered in calculation of profit or loss before tax – such as interest receipt or payment, dividend receipt in case of non-financing entity, etc.;

(*c*) Changes in inventories and **operating** receivables and payables;

(*d*) Actual income tax payment;

(*e*) Receipts/payments from extraordinary/exceptional items.

See the below format of cash flows from operating activities under indirect method:

Cash flows from operating activities	₹
Net profit before taxation and extraordinary items	XXXX
+/- Non-cash and non-operating items:	
Depreciation	XXX
Good will written off during the year	XXX
Interest income	(XXX)
Dividend income	(XXX)
Interest expense	XXX
Operating profit before working capital changes	**XXX**
Changes in operating assets and liabilities:	
Increase in sundry debtors	(XXX)
Decrease in inventories	XXX
Decrease in sundry creditors	(XXX)
Cash generated from operations	XXX
Income tax paid	(XXX)
Cash flow ***before*** special nature items (residuary)	**XXX**
Proceeds from earthquake disaster settlement	XXX
Net cash from operating activities	**XXX**

6. Interest and Dividends

An entity presents cash flows from operating, investing and financing activities in a manner which is most appropriate to its business.

The following are the examples of classification of various activities:

Particulars	**Classification for reporting cash flows**	
	Banks and financial institutions	**Other entities**
Interest received on loans and advances given	Operating	Investing
Interest paid on deposits and other borrowings	Operating	Financing
Interest and dividend received on investments in subsidiaries, associates and in other entities	Investing	Investing
Dividend paid on preference and equity shares, including tax on dividend paid on preference and equity shares by other entities	Financing	Financing
Finance charges paid by lessee under finance lease	Financing	Financing
Payment towards reduction of outstanding finance lease liability	Financing	Financing
Interest paid to vendor for acquiring fixed asset under deferred payment basis	Financing	Financing
Principal sum payment under deferred payment basis for acquisition of fixed assets	Investing	Investing
Penal interest received from customers for late payments	Operating	Operating
Penal interest paid to suppliers for late payments	Operating	Operating
Interest paid on delayed tax payments	Operating	Operating
Interest received on tax refunds	Operating	Operating

The total amount of interest paid during a period is disclosed in the statement of cash flows **whether** it has been recognised as an expense in P&L **or** capitalised in accordance with Ind AS 23 - Borrowing Costs.

CARVE OUTS - Ind AS 7 Vs. IAS 7- Statement of cash flow

Interest: In case of other than financial entities, IAS 7 gives an option to classify the interest paid and interest and dividends received as item of operating cash flows. Ind AS 7 does not provide such an option and requires these items to be classified as items of financing activity and investing activity, respectively.

Dividend: IAS 7 gives an option to classify the dividend paid as an item of operating activity. However, Ind AS 7 requires it to be classified as a part of financing activity only.

Concept capsule 7

Entity A constructs a machine (that is a qualifying asset under Ind AS 23) and pays construction expenses of ₹ 1,000, which includes ₹ 50 of capitalised interest. The entity paid ₹ 120 interest in the year, including the amount capitalised. Classify the cash flows.

Suggested answer

As per Ind AS 7, Interest paid should be classified as financing activity in case of other than financial institutions. Hence the entity should recognise ₹ 950 as an investing cash flow and ₹ 120 as financing cash flow. In addition, the total amount of ₹ 120 interest paid is disclosed in a note regarding how much is paid towards capitalisation of borrowing costs and other interest.

7. Income-tax

- **Income tax payment** shall be classified under **operating activities** unless they can be specifically identified with financing and investing activities. It is often ***impracticable to separate tax*** payments between operating and other than operating activities.
- If it is practicable to separate the tax payments among different activities, it should be separated and presented accordingly under the respective activity.

- When tax cash flows are allocated over more than one class of activity, the total amount of taxes paid is disclosed.

Concept capsule 8

During the financial year 2019-2020, Akola Limited have paid various taxes & reproduced the below mentioned records for your perusal:

- Capital gain tax of ₹ 20 crore on sale of office premises at a sale consideration of ₹ 100 crore.
- Income Tax of ₹ 3 crore on Business profits amounting ₹ 30 crore (assume entire business profit as cash profit).
- Dividend Distribution Tax of ₹ 2 crore on payment of dividend amounting ₹ 20 crore to its shareholders.
- Income tax Refund of ₹ 1.5 crore (Refund on taxes paid in earlier periods for business profits).

You need to determine the net cash flow from operating activities, investing activities and financing activities of Akola Limited as per relevant Ind AS. ***(ICAI Study material)***

Suggested answer

As per Ind AS 7, when it is practicable to identify the tax cash flow with an individual transaction that gives rise to cash flows that are classified as investing or financing activities the tax cash flow is classified as an investing or financing activity as appropriate. When tax cash flows are allocated over more than one class of activity, the total amount of taxes paid is disclosed.

Accordingly, the transactions are analysed as follows:

Particulars	Amount (in crore)	Activity
Sale Consideration	100	Investing Activity
Capital Gain Tax	(20)	Investing Activity
Business profits	30	Operating Activity
Tax on Business profits	(3)	Operating Activity
Dividend Payment	(20)	Financing Activity
Dividend Distribution Tax	(2)	Financing Activity
Income Tax Refund	1.5	Operating Activity
Total Cash flow	**86.5**	

Activity wise	**Amount (in crore)**
Operating Activity	28.5
Investing Activity	80
Financing Activity	(22)
Total	**86.5**

8. Cash flows in foreign currency

Receipts and payments of foreign currencies should be converted into the **functional currency** (*i.e.*, Read either Basic concepts **OR** Ind AS 21) using the exchange rate on the **date of cash flow**. Entities can use any rate which approximates to the actual rate.

UNREALISED foreign exchange gain or loss are **non**-cash items, hence **excluded** from statement of cash flow.

However, the effect of exchange rate **changes on cash and cash equivalents held or due in a foreign currency** is reported in the Statement of cash flows in order to reconcile cash and cash equivalents at the beginning and the end of the period. This amount is presented separately from Statement of cash flows and includes the differences, if any, had those cash flows been reported at end of period exchange rates.

Concept capsule 9

Raja Ltd. (whose functional currency is Rupees) has a foreign subsidiary entity B, based in the USA. Entity B has an opening balance of inventory of $240 and a closing balance of $270. At the start of the year, the exchange rate is $1 = ₹ 60 ($1.60), the closing rate is $1 = ₹ 63 ($1.80) and the average rate for the year is $1 = ₹ 61 ($1.65).

Suggested answer

As per Ind AS 7 - cash flows of the foreign subsidiary are translated at the actual exchange rate at the time of the transaction, or at an average exchange rate if that is a suitable approximation.

The simplest way of presenting the change in inventory of the foreign subsidiary is to identify the change in the subsidiary's foreign currency cash flows and translate that at the average rate, i.e., $30 (270 – 240) @61= ₹ 1,830. This amount is included in the changes in working capital presented in the reconciliation of net cash flows from operating activities using the indirect method.

This can be reconciled as follows:

Inventories at end of year ($270 @ 63) = ₹ 17,010

Inventories at beginning of year ($240 @ 60) = ₹ 14,400

Change in inventory $30 – Exchange difference:

Retranslation of opening balance at closing rate ($240 @60 – $240 @ 63) = ₹ 2,610

Retranslation of movement included in profit or loss ($30 @ 60 – $30 @ 63) = ₹ 90

Increase in inventories reported in the Statement of Cash Flows ₹ 2,610

9. Investments in subsidiaries, associates and joint ventures

When accounting for an investment in an associate, a joint venture or a subsidiary accounted for by use of the equity or cost method, an investor restricts its reporting in the SCF to the cash flows between itself and the investee, for example, to dividends and advances.

An entity that reports its interest in an associate or a joint venture using the equity method includes in its SCF the cash flows in respect of its investments in the associate or joint venture, and distributions and other payments or receipts between it and the associate or joint venture.

Acquisition and disposal of subsidiaries and other business units

The aggregate cash flows arising from acquisitions and from disposals of subsidiaries or other business units should be presented **separately** under investing activities. It means cash inflows from disposal should NOT be deducted outflows of acquisitions.

In the case of acquisition and disposal, the entity should disclose the following:

(*a*) The total purchase consideration received or paid;

(*b*) Cash and cash equivalents paid/received as part of consideration;

(*c*) the amount of cash and cash equivalents in the subsidiaries or other businesses over which control is obtained or lost; and

(*d*) the amount of the assets and liabilities other than cash or cash equivalents in the subsidiaries or other businesses, over which control is obtained or lost, summarised by each major category.

Point (c & d) need not be disclosed when the investment in subsidiary is measured at FVTPL.

Changes in ownership interests in a subsidiary that do not result in a loss of control, *such as the subsequent purchase or sale by a parent of a subsidiary's equity instruments*, are accounted for as equity transactions (see Ind AS 110) and presented as financing activities in SCF, unless the subsidiary is held by an investment entity and is required to be measured at fair value through profit or loss.

Accordingly, the resulting cash flows are classified as cash flows from financing activities.

10. Non-cash items

Investing and financing transactions that do not require the use of cash or cash equivalents shall be excluded from an SCF. Such transactions shall be disclosed elsewhere in the financial statements in a way that provides all the relevant information about these investing and financing activities.

Examples of non-cash transactions are:

(*a*) the acquisition of assets either by assuming directly related liabilities or by means of a lease;

(*b*) the acquisition of an entity by means of an equity issue; and

(*c*) the conversion of debt to equity.

Concept capsule 10

(This requires some knowledge of Ind AS 116 – Leases)

Rajani Ltd. is a manufacturing company. It obtains a new machine to use within its manufacturing plant under a 5-year lease agreement. The entity recognises the right-of-use asset within PPE at an amount of ₹ 4,00,000 and recognises a lease liability for ₹ 4,00,000. During the next financial year, it has paid scheduled repayments of ₹ 35,000, of which ₹ 2,900 was recognised as a finance cost in P&L. It has a policy of recognising interest paid within financing activities. Comment.

Suggested answer

The addition to PPE of ₹ 4,00,000 will be shown as a non-cash transaction in the notes to the financial statements because there is no immediate cash flow involved at the inception of the lease. The creation of the ₹ 400,000 lease liability is not shown as a financing inflow but is instead disclosed in the non-cash transactions note.

In the next year, ₹ 2,900 interest element of the lease rentals is included in the total of interest paid within financing activities in accordance with the entity's accounting policy and the ₹ 32,100 (₹ 35,000 – ₹ 2,900) capital element of the lease rentals paid will be classified as a financing outflow in accordance with.

Concept capsule 11

Entity D acquired a subsidiary on 1st October, 2016. Consideration of ₹ 10,00,000 recognised at the date of acquisition consisted of:

- Cash – ₹ 4,50,000
- Present value of deferred consideration payable in 6 months – ₹ 2,25,000
- Fair value of contingent consideration – ₹ 3,25,000. The actual amount payable depends on whether certain revenue and profit targets are met over the following year.

The identifiable net assets of the newly acquired subsidiary included cash and cash equivalents of ₹ 140,000.

How is this acquisition reflected in the Statement of Cash Flows for the year ended 31st March, 2017?

Suggested answer

1. a Net cash outflow of ₹ 3,10,000 is reported as cash flows from investing activities, being the cash consideration paid of ₹ 4,50,000 less the cash and cash equivalents acquired of ₹ 1,40,000.

2. The deferred and contingent consideration amounts of ₹ 2,25,000 and ₹ 3,25,000 are non-cash transactions, as no cash has yet been paid. These amounts are excluded from the Statement of Cash Flows but will be reported as part of the total consideration disclosure.

11. Components of cash and cash equivalents

An entity shall **disclose:**

- **The components** of cash and cash equivalents
- Reconciliation between cash & cash equivalents in SCF and the items reported in balance sheet;
- The policy which it adopts in determining the composition of cash and cash equivalents; and
- If there is any change in such policy, it should be reported as per Ind AS 8.

12. Disclosures

- The amount of significant cash and cash equivalent balances held by the enterprise those are NOT available for use by it and management's comment should be added to that.
    - *Example:* cash and cash equivalent balances held by a branch of the entity which operates in a foreign country where exchange controls or other legal restrictions apply as a result of which the balances are not available for use by the entity.
- Any additional information may be relevant to users in understanding the financial position and liquidity of an enterprise.
- The disclosure of segmental cash flows enables users to obtain a better understanding of the relationship between the cash flows of the business as a whole and those of its component parts and the availability and variability of segmental cash flows.

QUESTIONS & ANSWERS

Question No. 1 (Little knowledge in SFM is required to understand the terminology)

Classify the following transactions into operating or investing or financing activities.

1. Cancellation of forward contract for payment against imported raw materials.
2. Settlement of futures contract by way of a hedge against risk in an investment portfolio.
3. Forward rate agreement for remittance of dividends to NRIs.

Answer

1. Operating activities – As forward contract is directly related to operating activities.
2. Investing activities – As future contract is directly related to investments.
3. Financing activities – As the agreement is related to payment of dividends.

Question No. 2

Entity A is a property company. During the year it has secured ₹ 5 million of finance, which is ring-fenced for use only for a specific development. The funds are held in a designated bank deposit account to be used only for the purposes of the specific development project, which is expected to take 3 years to complete. Withdrawals from the account can only be made with the approval of the lender when specified milestones are met. At the year end, ₹ 1 million of the fund has been used on the development and ₹ 4 million remains in the designated account.

Answer

In this situation, the money has been obtained in order to support long-term cash needs, being the completion of the development over the three-year period. Although the designated account may not have a specified term, withdrawals can only be made to pay for actual expenditure when certain conditions are met on the specified project, which is expected to occur over the three-year lifespan of the project. Consequently, the account is not available 'on demand' and is not available to meet short-term cash commitments. Consequently, it will not meet the definition of cash equivalents. The balance in the designated account at the reporting date is likely to be included in the 'cash at bank' line item in the statement of financial position so adequate disclosure on the amount of and the reasons for the restrictions should be given in a note.

Question No. 3

How do you classify cash receipts and payments arising out of future contracts, forward contracts, option contracts and swap contracts? *(Requires Hedge accounting knowledge of Ind AS 109 – Financial instruments)*

Answer

Paragraph 16 of Ind AS 7, amongst other examples of cash flows arising from investing activities, provides as follows:–

"(*g*) cash payments for future contracts, forward contracts, option contracts and swap contracts except when the contracts are **held for dealing or trading purposes**, or the payments are classified as financing activities; and

(*h*) cash receipts from future contracts, forward contracts, option contracts and swap contracts except when the contracts are **held for trading purposes**, or the receipts are classified as financing activities.

When a contract is accounted for as a hedge of an identifiable position the cash flows of the contract are classified in the same manner as the cash flows of the position being hedged."

From the above paragraphs, it is clear that classification of cash flows from future contracts, forward contracts, option contracts and swap contracts depends on whether a contract is accounted for as a hedging instrument for hedged item or not.

When such a contract is accounted for as a hedge, cash flows arising from hedging instruments are classified as operating, investing or financing activities, on the basis of the classification of the cash flows arising from the hedged item. *Example:* When a forward contract is taken for repayment of a foreign currency loan and hedge accounting is followed, cash payments and receipts of the aforesaid forward contract is classified as financing activities.

When these contracts are not accounted for as hedge, the classification of cash flows depends on the nature of the contract itself, *i.e.*, if these contracts are held for dealing or trading purposes, cash flows arising from such transactions should be classified as cash flows from operating activities. Otherwise, the cash flows will be classified as investing activities except where cash flows are classified as financing activities.

Question No. 4

Z Ltd. has no foreign currency cash flow for the year 2017. It holds some deposit in a bank in the USA. The balances as on 31.12.2017 and 31.12.2018 were US$ 100,000 and US$ 102,000 respectively. The exchange rate on December 31, 2017 was US$1 = ₹ 45. The same on 31.12.2018 was US$1 = ₹ 50. The increase in the balance was on account of interest credited on 31.12.2018. Thus, the deposit was reported at ₹ 45,00,000 in the balance sheet as on December 31, 2017. It was reported at ₹ 51,00,000 in the balance sheet as on 31.12.2018. How these transactions should be presented in cash flow for the year ended 31.12.2018 as per Ind AS 7?

Answer

The profit and loss account was credited by ₹ 1,00,000 (US$ 2000 × ₹ 50) towards interest income. It was credited by the exchange difference of US$ 100,000 × (₹ 50 – ₹ 45) that is, ₹ 5,00,000. In preparing the cash flow statement, ₹ 5,00,000, the exchange difference, should be deducted from the 'net profit before taxes, and extraordinary item'. However, in order to reconcile the opening balance of the cash and cash equivalents with its closing balance, the exchange difference ₹ 5,00,000, should be added to the opening balance in note to cash flow statement.

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

Question No. 5

Company A acquires 70% of the equity stake in Company B on July 20, 20X1. The consideration paid for this transaction is as below:

(*a*) Cash consideration of ₹ 15,00,000

(*b*) 200,000 equity shares having face of ₹ 10 and fair value of ₹ 15 per share.

On the date of acquisition, Company B has cash and cash equivalent balance of ₹ 2,50,000 in its books of account.

On October 10, 20X2, Company A further acquires 10% stake in Company B for cash consideration of ₹ 8,00,000.

Advise how the above transactions will be disclosed/presented in the statement of cash flows as per Ind AS 7.

Answer

As per Ind AS 7, the aggregate cash flows arising from obtaining control of subsidiary shall be presented separately and classified as investing activities.

As per Ind AS 7, cash flows arising from changes in ownership interests in a subsidiary that do not result in a loss of control shall be classified as cash flows from financing activities, unless the subsidiary is held by an investment entity, as defined in Ind AS 110, and is required to be measured at fair value through profit or loss. Such transactions are accounted for as equity transactions and accordingly, the resulting cash flows are classified in the same way as other transactions with owners.

Considering the above, for the financial year ended March 31, 20X2 total consideration of ₹ 15,00,000 less ₹ 250,000 will be shown under investing activities as "Acquisition of the subsidiary (net of cash acquired)".

There will not be any impact of issuance of equity shares as consideration in the cash flow statement however a proper disclosure shall be given elsewhere in the financial statements in a way that provides all the relevant information about the issuance of equity shares for non - cash consideration.

Further, in the statement of cash flows for the year ended March 31, 20X3, cash consideration paid for the acquisition of additional 10% stake in Company B will be shown under financing activities.

Question No. 6

From the following data of Galaxy Ltd., prepare statement of cash flows showing cash generated from Operating Activities using direct method as per Ind AS 7:

	31.3.20X2 (₹)	**31.3.20X1 (₹)**
Current Assets:		
Inventory	1,20,000	1,65,000
Trade receivables	2,05,000	1,88,000
Cash & cash equivalents	35,000	20,500
Current Liabilities:		
Trade payable	1,95,000	2,15,000
Provision for tax	48,000	65,000

Summary of Statement of Profit and Loss		₹
Sales	85,50,000	
Less: Cost of sales	(56,00,000)	29,50,000
Other Income		
Interest income	20,000	
Fire insurance claim received	1,10,000	1,30,000
		30,80,000
Depreciation	(24,000)	
Administrative and selling expenses	(15,40,000)	
Interest expenses	(36,000)	
Foreign exchange loss	(18,000)	(16,18,000)
Net Profit before tax and extraordinary income		14,62,000
Income Tax		(95,000)
Net Profit		**13,67,000**

Additional information:

(*i*) Trade receivables and Trade payables include amounts relating to credit sale and credit purchase only.

(*ii*) Foreign exchange loss represents increment in liability of a long-term borrowing due to exchange rate fluctuation between acquisition date and balance sheet date.

Answer

Statement Cash Flows from operating activities of Galaxy Ltd. for the year ended 31 March 20X2 (Direct Method)

Particulars	₹	₹
Operating Activities:		
Cash received from Trade receivables (W.N. 3)		85,33,000
Less: Cash paid to Suppliers (W.N.2)	55,75,000	
Payment for Administration and Selling expenses	15,40,000	
Payment for Income Tax (W.N.4)	1,12,000	(72,27,000)
		13,06,000
Adjustment for exceptional items (fire insurance claim)		1,10,000
Net cash generated from operating activities		14,16,000

Working Notes:

1. **Calculation of total purchases**

   Cost of Sales = Opening stock + Purchases – Closing Stock =₹ 56,00,000 = ₹ 1,65,000 + Purchases – ₹ 1,20,000;

   So, purchases = ₹ 55,55,000

2. Calculation of cash paid to Suppliers

Trade Payables

	₹		₹
To Bank A/c (b/f)	55,75,000	By Balance b/d	2,15,000
To Balance c/d	1,95,000	By Purchases (W.N. 1)	55,55,000
	57,70,000		57,70,000

3. Calculation of cash received from Customers

Trade Receivables

	₹		₹
To Balance b/d	1,88,000	By Bank A/c (balancing figure)	85,33,000
To Sales	85,50,000	By Balance c/d	2,05,000
	87,38,000		87,38,000

4. Calculation of tax paid during the year in cash

Provision for tax

	₹		₹
To Bank A/c (balancing figure)	1,12,000	By Balance b/d	65,000
To Balance c/d	48,000	By Profit and Loss A/c	95,000
	1,60,000		1,60,000

Question No. 7 ***(CA Final – Dec. 2021)***

In the year 2020-2021, one land was sold for ₹ 5 crore and another land purchased for ₹ 3 crore by XYZ Limited. Company reported Cash Flow on a Net Basis in Cash Flow Statement *i.e.* ₹ 2 crore in Investing Activity as Cash receipt from Sale of Land. Advise whether treatment given as above is correct or not as per the provisions of Ind AS 7.

Also, calculate the cash from operations by indirect method from the following information:

Operating Statement of XYZ Limited for the year ended 31st March, 2021

Particulars	₹
Sales	*20,00,000*
Less: Cost of goods sold	*(14,00,000)*
Administration & selling overheads	*(2,20,000)*
Depreciation	*(28,000)*
Interest paid	*(12,000)*
Loss on sale of asset	*(8,000)*
Profit before tax	*3,32,000*
Less: Tax	*(1,20,000)*
Profit after tax	*2,12,000*

Balance Sheet as on 31st March

	2021 (₹)	*2020 (₹)*
Assets		
Non-current assets		
Property, plant and equipment	*3,00,000*	*2,60,000*
Investment	*48,000*	*40,000*

	2021 (₹)	2020 (₹)
Current assets		
Inventories	*48,000*	*52,000*
Trade receivables	*40,000*	*28,000*
Cash and cash equivalents	*24,000*	*20,000*
Total	***4,60,000***	***4,00,000***
Equity and liabilities		
Share holders' funds	*2,40,000*	*2,00,000*
Non-current Liabilities	*1,32,000*	*1,40,000*
Current liabilities		
Trade payables	*48,000*	*32,000*
Expenses payables	*40,000*	*28,000*
Total	***4,60,000***	***4,00,000***

Answer

(*i*) Correct treatment of cash flow:

If nothing is specifically mentioned, then as per Ind AS 7, the cash flows will be presented on gross basis. Gross basis means the receipts would be shown separately and the payments will be shown separately.

Accordingly, in the year 2020-2021, while presenting the information, entity will show separately cash outflow from investing activity of ₹ 3 crore for purchase of land and cash inflow from investing activity of ₹ 5 crore from sale of land.

(*ii*) Cash flow from Operations by Indirect Method:

	₹
Profit After Tax	2,12,000
*Add back/(Less):*Depreciation	28,000
Interest paid	12,000
Loss on sale of an asset	8,000
Adjustments for changes in inventory and operating receivables and payables	2,60,000
Decrease in inventory	4,000
Increase in trade receivables	(12,000)
Increase in trade payables	16,000
Increase in expenses payables	12,000
Net cash generated from operating activity	2,80,000

"Train your mind to see the good in every situation."

– Lord Buddha

Ind AS 7: Statement of Cash Flows

↓

Presentation of flow of cash & cash equivalents during the year

↓

Cash activity

Operating activities	Investing activities	Financing activities
Principal revenue producing activities & other than Investing and financing activities	Acquisition & disposal of long term assets & others (other than cash equivalents)	Which changes the composition or size of owner's capital/borrowing

Net basis reporting
- Cash flows from customers
- Items of quick turnover, short maturity & large amounts

Present on Gross basis subject to exceptions
IA and FA are same as direct method

Operating activity presentation

↓

2 methods

Direct method (preferred method)

Major classes of gross cash receipts & cash payments are disclosed

Difference is there only in presentation of operating activities.

Indirect method

Net profit before tax	
+/- Non cash & non-operating items	xx
+/- changes in working capital	xx
- Tax paid	xx
	xx

Important points

- Bank OD - integral part of cash management - include in as cash & cash equivalent and **not** as a financing activity;
- A single transaction may include cash flows that are classified differently.
  E.g. in case if a Fixed asset is acquired on deferral payment basis, then the instalment payment in respect of such fixed asset should be split and interest element on such fixed asset should be classified as financing activity and repayment of loan amount to be classified as investing activity.

Disclosure
- Components of Cash & Cash equivalents;
- Reconciliation CFS numbers with reported in BS;
- Management comments on special areas;

Other considerations

- Cash flows must be reported on "gross" basis. Presentation on net basis is permitted only in very limited cases like cash receipts/payments made on behalf of customers (eg: rent collected on behalf of and paid over to owners of property), or where cash receipts/payments are for items in which turnover is quick, amounts are large and maturities are short (eg: purchase or sale of investments)
- Record foreign currency transactions in Functional currency using the rate on the date of cash flow.
- NO extraordinary items presentation;
- If equity method followed for investment in associate/JV, only cash flows between the entity and the investee will be reflected in the statement of cash flows
- Non-cash investing and financing transactions are **not to be disclosed** in the statement of cash flows though information relevant may be provided elsewhere in the Financial Statements.