



Date: 14 September 2021

VIRTUAL COACHING CLASSES ORGANISED BY BOS, ICAI

FINAL LEVEL PAPER 1: FINANCIAL REPORTING

TOPIC: IND AS 7 STATEMENT OF CASH FLOWS

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Objective of Ind AS 7

- To provide a statement to help investors assess the prospects for future cash flows, and to confirm or change their past expectations
- To require the provision of information about the historical changes in cash and cash equivalents of an entity which classifies cash flows during the period from operating, investing and financing activities.

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.

Cash and Cash Equivalents

- **Cash** comprises cash on hand and demand deposits.
- **Cash equivalents** are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Can include bank overdrafts if part of cash management activities and balance fluctuates between positive and negative amounts

Case Study- Cash & Cash Equivalents

Illustration 1

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:

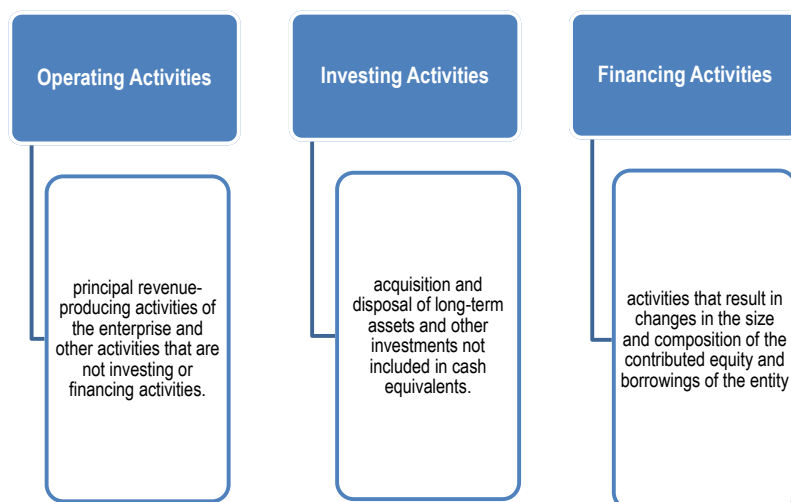
Sr. No.	Name of the Security	Additional Information
1.	Fixed deposit with SBI	12%, 3 years maturity on 1 st January 20X4
2.	Fixed deposit with HDFC	10%, original term was for 2 years, but due for maturity on 30 th June 20X1
3.	Redeemable Preference shares in ABC Ltd	Acquired on 31 st January 20X1 and the redemption is due on 30 th 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

Case Study- Cash & Cash Equivalents

Solution

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

Presentation of Cash Flow Statement



Operating Activities

- Indicates the extent to which the operations of the entity have generated sufficient cash flows to repay loans, maintain the operating capability of the entity, etc.

- **Operating cash flows:**

- Cash received from customers for the sale of goods and provision of services, or on account of royalties, fees, or commissions
- Cash payments to suppliers for goods and services provided; and to and on behalf of employees for their services
- Cash received from or paid for financial instruments held specifically for dealing or trading purposes

Case Study- Operating Cash Flows

Illustration 2

From the following transactions, identify which transactions will be qualified for the calculation of operating cash flows, if company is into the business of trading of mobile phones.

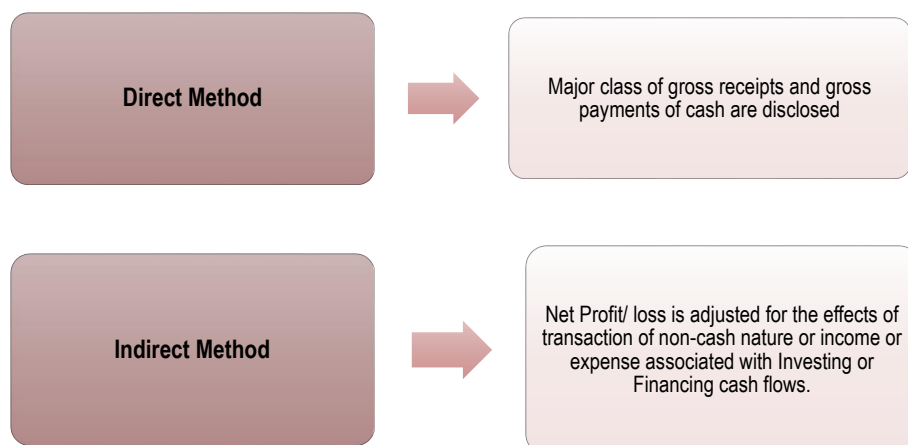
Sr. No.	Nature of Transaction
1	Receipt from sale of mobile phones
2	Purchases of mobile phones from various companies
3	Employees expenses paid
4	Advertisement expenses paid
5	Credit sales of mobile
6	Miscellaneous charges received from customers for repairs of mobiles
7	Loss due to decrease in market value of the closing stock of old mobile phones
8	Payment to suppliers of mobile phones
9	Depreciation on furniture of sales showrooms
10	Interest paid on cash credit facility of the bank
11	Profit on sale of old computers and printers, in exchange of new laptop and printer
12	Advance received from customers
13	Sales Tax and excise duty paid

Case Study- Operating Cash Flows

Solution

Sr. No.	Nature of Transaction	Included / Excluded with reason
1	Receipt from sale of mobile phones	Include – main revenue generating activity
2	Purchases of mobile phones from various companies	Include – expenses related to main operations of business
3	Employees expenses paid	Include – expenses related to main operations of business
4	Advertisement expenses paid	Include – expenses related to main operations of business
5	Credit sales of mobile	Do not include – Credit transaction will not be included in cash flow (receipts from customers will be included)
6	Misc. charges received from customers for repairs of mobiles	Include – supplementary revenue generating activity
7	Loss due to decrease in market value of the closing stock of old mobile phones	Do not include - Non cash transaction
8	Payment to suppliers of mobile phones	Include – cash outflow related to main operations of business
9	Depreciation on furniture of sales showrooms	Do not include – non cash item
10	Interest paid on cash credit facility of the bank	Do not include – cost of finance
11	Profit on sale of old computers and printers, in exchange of new laptop and printer	Do not include – non cash item
12	Advance received from customers	Include – Related to operations of business
13	Sales tax and excise duty paid	Include – related to operations of business

Operating Activities



Case Study- Methods of SCF

Illustration 6

Find out the cash from operations by direct method and indirect method from the following information:

Operating statement of ABC Ltd. for the year ended 31.3.20X2

Particulars	₹
Sales	5,00,000.00
Less: Cost of goods sold	3,50,000.00
Administration & Selling Overheads	55,000.00
Depreciation	7,000.00
Interest Paid	3,000.00
Loss on sale of asset	<u>2,000.00</u>
Profit before tax	83,000.00
Tax	<u>(30,000.00)</u>
Profit After tax	<u>53,000.00</u>

Case Study- Methods of SCF

Balance Sheet as on 31 st March		
	20X2	20X1
Assets		
Non-current Assets		
Property, Plant and Equipment	75,000.00	65,000.00
Investment	12,000.00	10,000.00
Current Assets		
Inventories	12,000.00	13,000.00
Trade receivables	10,000.00	7,000.00
Cash and cash equivalents	6,000.00	5,000.00
Total	1,15,000.00	1,00,000.00
Equity and Liabilities		
Shareholders' Funds	60,000.00	50,000.00
Non-current Liabilities	33,000.00	35,000.00
Current Liabilities		
Trade Payables	12,000.00	8,000.00
Payables for Expenses	10,000.00	7,000.00
Total	1,15,000.00	1,00,000.00

Case Study- Methods of SCF

Solution

1. Cash flow from Operations by Direct Method

Particulars	₹	See Note
Cash Sales	4,97,000.00	1
Less: Cash Purchases	3,45,000.00	2
Overheads	52,000.00	3
Interest	-	Financing
Depreciation	-	Non cash item
Loss on sale of asset	-	Investing item
Cash profit	100,000.00	
Less: Tax	(30,000.00)	
Cash profit after tax	70,000.00	

Note No 1 - Cash Receipts from Sales and Trade receivables

Particulars	₹
Sales	5,00,000.00
Add : Opening Trade receivables	7,000.00
Less : Closing Trade receivables	(10,000.00)
Cash Receipts	4,97,000.00

Case Study- Methods of SCF

Note No 2 :- Payment to Trade Payables for Purchases	
Particulars	₹
Cost of goods sold	3,50,000.00
Closing inventories	12,000.00
Less: Opening inventories	(13,000.00)
Purchases	3,49,000.00
Add: Opening Trade Payables	8,000.00
Less: Closing Trade Payables	(12,000.00)
Payment to creditors	<u>3,45,000.00</u>
Particulars	₹
Overheads	55,000.00
Add: Opening payables	7,000.00
Less: Closing payables	(10,000.00)
Payment for Overheads	<u>52,000.00</u>

Case Study- Methods of SCF

2. Cash flow from Operations by Indirect Method

Indirect Method	₹
Profit After Tax	53,000.00
Add/(Less): Depreciation	7,000.00
Loss on Asset	2,000.00
Interest paid	3,000.00
Decrease in Inventory	1,000.00
Increase in Trade Receivables	(3,000.00)
Increase in Trade Payables	4,000.00
Increase in Payables for expenses	<u>3,000.00</u>
Total	<u>70,000.00</u>

Note: Cash flow derived from operations ₹ 70,000 is same in both Direct Method and Indirect Method.

Investing Activities

- It represents the extent to which expenditures have been made for resources intended to generate future income and cash flows.

■ Investing cash flows:

- Cash payments to acquire and cash receipts from the disposal of property, plant and equipment, intangibles, and other long-term assets, including capitalized development costs
- Cash payments to acquire and cash receipts from the disposal of debt and equity instruments of other entities or interests in joint ventures, excluding investments held for trading or in cash equivalents
- Cash advances and loans to other parties and their cash repayments
- Cash payments for and receipts from futures, forwards, options and swaps unless they are held for trading or are classified as financing flows.

Case Study- Investing Cash Flows

Illustration 3

From the following transactions taken from a private sector bank operating in India, identify which transactions will be classified as operating and which would be classified as Investing activity.

S. No.	Nature of transaction paid
1	Interest received on loans
2	Interest paid on Deposits
3	Deposits accepted
4	Loans given to customers
5	Loans repaid by the customers
6	Deposits repaid
7	Commission received
8	Lease rentals paid for various branches
9	Service tax paid
10	Furniture purchased for new branches
11	Implementation of upgraded banking software
12	Purchase of shares in 100% subsidiary for opening a branch in Abu Dhabi
13	New cars purchased from Honda dealer, in exchange of old cars and remaining amount paid in cash
14	Provident fund paid for the employees
15	Issued employee stock options

Case Study- Investing Cash Flows

Solution

Sr. No.	Nature of transaction paid	Operating / Investing / Not to be considered
1	Interest received on loans	Operating – Main revenue generating activity
2	Interest paid on Deposits	Operating – Main expenses of operations
3	Deposits accepted	Operating – in case of financial institutes
4	Loans given to customers	Operating – in case of financial institutes
5	Loans repaid by the customers	Operating – in case of financial institutes
6	Deposits repaid	Operating – in case of financial institutes
7	Commission received	Operating – Main revenue generating activity
8	Lease rentals paid for various branches	Operating – Main expenses of operations
9	Service tax paid	Operating – Main expenses of operations
10	Furniture for new branches	Investing – Assets purchased
11	Implementation of upgraded banking software	Investing – Purchased for long term purpose
12	Purchase of shares in 100% subsidiary for opening a branch in Abu Dhabi	Investing – strategic investment
13	New cars purchased from Honda dealer, in exchange of old cars and cash payment	Investing-for cash payment
14	Provident fund paid for the employees	Operating
15	Issued employee stock options	Not to be considered. No cash flow

Financing Activities

- “Result in changes in the size and composition of the contributed equity and borrowings of the entity”

- It helps in predicting claims on future cash flows by providers of capital to the entity.

■ Financing cash flows:

- Cash proceeds from issuing shares or other equity instruments;
- Cash payments to owners to acquire or redeem the entity’s shares;
- Cash proceeds from issuing debentures, loans, notes, bonds, mortgages and other short-term or long-term borrowings;
- Cash repayments of amounts borrowed; and
- Payment by a lessee for the reduction of the outstanding liability relating to a lease.

Case Study- Financing Cash Flows

Illustration 4

From the following transactions taken from a parent company having multiple businesses and multiple segments, identify which transactions will be classified as Operating, Investing and Financing:

Sr. No.	Nature of transaction
1	Issued preference shares
2	Purchased the shares of 100% subsidiary company
3	Dividend received from shares of subsidiaries
4	Dividend received from other companies
5	Bonus shares issued
6	Purchased license for manufacturing of special drugs
7	Royalty received from the goods patented by the company
8	Rent received from the let out building (letting out is not main business)
9	Interest received from loans and advances given
10	Dividend paid
11	Interest paid on security deposits
12	Purchased goodwill
13	Acquired the assets of a company by issue of equity shares (not parting any cash)
14	Interim dividends paid
15	Dissolved the 100% subsidiary and received the amount in final settlement

Case Study- Financing Cash Flows

Solution

Sr. No.	Nature of transaction	Operating / Investing / Financing / Not to be considered
1	Issued preference shares	Financing
2	Purchased the shares of 100% subsidiary company	Investing
3	Dividend received from shares of subsidiaries	Investing
4	Dividend received from other companies	Investing
5	Bonus shares issued	No cash flow
6	Purchased license for manufacturing of special drugs	Investing
7	Royalty received from the goods patented by the company	Operating
8	Rent received from the let out building (letting out is not main business)	Investing
9	Interest received from loans and advances given	Investing
10	Dividend paid	Financing
11	Interest paid on security deposits	Financing
12	Purchased goodwill	Investing
13	Acquired the assets of a company by issue of equity shares (not parting any cash)	Not to be considered
14	Interim dividends paid	Financing
15	Dissolved the 100% subsidiary and received the amount in final settlement	Investing

Classification of Interest and dividends

Particulars	Financial Institution	Other Entities
Interest received	Operating activities	Investing activities
Interest paid	Operating activities	Financing activities
Dividends received	Operating activities	Investing activities
Dividends paid	Financing activities	Financing activities

Case Study- Interest Received

Illustration 7

A firm invests in a five-year bond of another company with a face value of ₹ 10,00,000 by paying ₹ 5,00,000. The effective rate is 15%. The firm recognises proportionate interest income in its income statement throughout the period of bond.

Based on the above information answer the following question:

- How the interest income will be treated in cash flow statement during the period of bond?
- On maturity, whether the receipt of ₹ 10,00,000 should be split between interest income and receipts from investment activity.

Solution

Interest income will be treated as income over the period of bond in the income statement. However, there will be no cash flow in these years because no cash has been received. On maturity, receipt of ₹ 10,00,000 will be classified as investment activity with a bifurcation of interest income & money received on redemption of bond.

Specific Points:

➤ 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.

➤ No netting of inflows and outflows

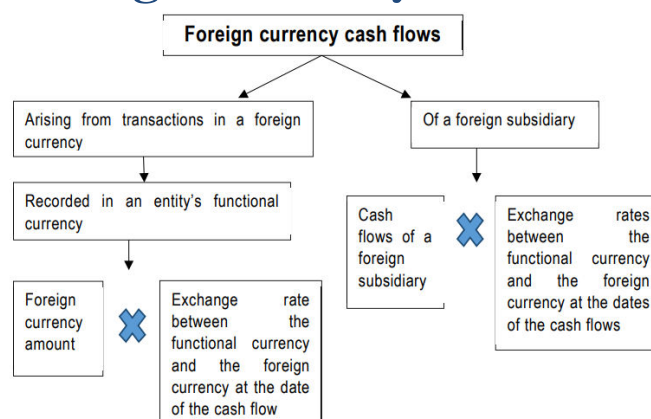
➤ Income tax cash flows – Generally reported as operating cash flows

➤ Non-cash transactions – Not included in statement, instead disclosed elsewhere

➤ Acquisition/loss of control of subsidiary – Classified as Investing cash flow

➤ Change in ownership interests in a subsidiary not resulting in loss of control - Classified as Financing cash flow

Summary- Foreign Currency Cash Flows



Note:

1. Cash flows denominated in a foreign currency are reported in a manner consistent with Ind AS 21.
2. A weighted average exchange rate for a period may be used for recording foreign currency transactions or the translation of the cash flows of a foreign subsidiary
3. Ind AS 21 does not permit use of the exchange rate at the end of the reporting period when translating the cash flows of a foreign subsidiary

Case Study- Foreign Currency Cash Flows

Example 3

Entity A (Indian Company) purchased goods for resale from France during January for EUR 10,000 (Exchange rate: 1 EUR = ₹ 70) on a credit period of 4 months. It accounted for the purchase of inventory at ₹ 7,00,000 (10,000 x 70). On 31st March, the exchange rate has changed to 1 EUR = ₹ 65. This would mean an unrealised gain due to exchange fluctuation of ₹ 50,000 (since the payables will be recorded at ₹ 6,50,000 (at closing exchange rate)).

Assuming that the inventory is unsold at that date, the movement is reported as under:

Profit	₹ 50,000
Less: Increase in Inventory	₹ (7,00,000)
Add: Increase in Payables	₹ <u>6,50,000</u>
Net Cash flows from operating activities	₹ <u>0</u>

Case Study- Taxes on Income

Illustration 8

X Limited has paid an advance tax amounting to ₹ 5,30,000 during the current year. Out of the above paid tax, ₹ 30,000 is paid for tax on long term capital gains.

Under which activity the above said tax be classified in the cash flow statements of X Limited?

Solution

Cash flows arising from taxes on income should be classified as cash flows from operating activities unless they can be specifically identified with financing and investing activities. In the case of X Limited, the tax amount of ₹ 30,000 is specifically related with investing activities. ₹ 5,00,000 to be shown under operating activities. ₹ 30,000 to be shown under investing activities.

Case Study- Non Cash Transaction

Illustration 9

X Limited acquires fixed asset of ₹ 10,00,000 from Y Limited by accepting the liabilities of ₹ 8,00,000 of Y Limited and balance amount it paid in cash. How X Limited will treat all those items in its cash flow statements?

Solution

Investing and financing transactions that do not require the use of cash and cash equivalents shall be excluded from a statement of cash flows. X Limited should classify cash payment of ₹ 2,00,000 under investing activities. The non-cash transactions –liabilities and asset should be disclosed in the notes to the financial statements.

Disclosures:

➤ Components of cash and cash equivalents:

An entity is required to:

- disclose the components of cash and cash equivalents and a reconciliation of the amounts in its statement of cash flow with Balance sheet items.
- disclose the policy adopted in determining the composition of cash and cash equivalents as per Ind AS 1, Presentation of Financial Statements
- effect of any change in the policy for determining components of cash and cash equivalents

Case Study- Components of Cash and Cash Equivalents

Illustration 10

An entity has bank balance in foreign currency aggregating to USD 100 (equivalent to ₹ 4,500) at the beginning of the year. Presuming no other transaction taking place, the entity reported a profit before tax of ₹ 100 on account of exchange gain on the bank balance in foreign currency at the end of the year. What would be the closing cash and cash equivalents as per the balance sheet?

Case Study- Components of Cash and Cash Equivalents

Solution

For the purpose of statement of cash flows, the entity shall present the following:

	Amount (₹)
Profit before tax	100
Less: Unrealised exchange gain	(100)
Cash flow from operating activities	Nil
Cash flow from investing activities	Nil
Cash flow from financing activities	Nil
Net increase in cash and cash equivalents during the year	Nil
Add: Opening balance of cash and cash equivalents	4,500
Cash and cash equivalents as at the year-end	4,500

Reconciliation of cash and cash equivalents

Cash and cash equivalents as per statement of cash flows	4,500
Add: Unrealised gain on cash and cash equivalents	100
Cash and cash equivalents as per the balance sheet	4,600

If any changes in the policies take place, that will be dealt with as per the provisions of Ind AS 8.

Other Disclosures:

➤ Other disclosures:

- Disclose the amount and commentary of management in respect of significant cash and cash equivalent balances held by the entity that are not available for use by the group. There are various circumstances in which balances of cash and cash equivalent held by an entity are not available for use by the group.
- Additional information may be relevant to users in understanding the financial position and liquidity of an entity. Disclosure of this information with a commentary by management is encouraged in the following:-
 - ✓ the amount of undrawn borrowing facilities available for future operating activities or to settle capital commitments, indicating any restrictions on the use of these facilities;
 - ✓ the aggregate amount of cash flows that represent increases in operating capacity separately from those cash flow to maintain operating capacity; and
 - ✓ Cash flow arising from the operating activities, investing activities & financing activities of each reportable segment (see Ind AS 108, Operating Segments).
- Disclosure of cash flows that represent increases in operating capacity and cash flow to maintain operating capacity is useful to understand whether it invests adequately in the maintenance of its operating capacity or is possibly prejudicing future profitability for the sake of current liquidity and distributions to owners.
- Disclosure of segmental cash flows enables users to understand 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 flow.

Key Differences:

Particulars	Ind AS 7	AS 3
Bank Overdrafts	Included as Cash and Cash Equivalents if they are an integral part of entity's cash management	Financing activities
Cash flows from extraordinary items	Not shown	Classified as operating, financing or investing and separately disclosed
Investing Activities	Only expenses that result in recognition of an asset are shown in Investment	No specific guidance
Presentation	More guidance	Comparatively less guidance



THANK YOU

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18 September
2021

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