Cash Flow Statement

6

Learning Objectives

After studying this chapter, you will be able to :

- *State the purpose and preparation of statement of cash flow statement;*
- *Distinguish between operating activities, investing activities and financing activities;*
- *Prepare the statement of cash flows using direct method;*
- *Prepare the cash flow statement using indirect method.*

Till now you have learnt about the financial statements being primarily inclusive of Position Statement (showing the financial position of an enterprise as on a particular date) and Income Statement (showing the result of the operational activities of an enterprise over a particular period). There is also a third important financial statement known as *Cash flow statement,* which shows inflows and outflows of the cash and cash equivalents. This statement is usually prepared by companies which comes as a tool in the hands of users of financial information to know about the sources and uses of cash and cash equivalents of an enterprise over a period of time from various activities o*f an enterprise.* It has gained substantial importance in the last decade because of its practical utility to the users of financial information.

Accounting Standard-3 (AS-3), issued by The Institute of Chartered Accountants of India (ICAI) in june 1981, which dealt with a statement showing 'Changes in Financial Position', (Fund Flow Statement), has been revised and now deals with the preparation and presentation of Cash flow statement. The revised AS-3 has made it mandatory for all listed companies to prepare and present a cash flow statement along with other financial statements on annual basis. Hence, it may be noted, that Fund Flow statement is no more considered relevant in accounting and so not discussed here.

A cash flow statement provides information about the historical changes in cash and cash equivalents of an enterprise by classifying cash flows into operating, investing and financing activities. It requires that an enterprise should prepare a cash flow statement and should present it for each accounting period for which financial statements are presented. You will recall that cash flow analysis has also been mentioned in Chapter 4 as a technique of financial analysis. This chapter discusses this technique and explains the method of preparing a cash from statement for an accounting period.

6.1 Nature of Cash Flow Statement

A Cash flow statement shows inflow and outflow of cash and cash equivalents from various activities of a company during a specific period. The primary objective of cash flow statement is to provide useful information about cash flows (inflows and outflows) of an enterprise during a particular period under various heads, i.e. operating activities, investing activities and financing activities.

This information is useful in providing users of financial statements with a basis to assess the ability of the enterprise to generate cash and cash equivalents and the needs of the enterprise to utilise those cash flows. The economic decisions that are taken by users require an evaluation of the ability of an enterprise to generate cash and cash equivalents and the timing and certainty of their generation.

6.2 Benefits of Cash Flow Statement

Cash flow statement provides the following benefits :

- A cash flow statement when used along with other financial statements provides information that enables users to evaluate changes in net assets of an enterprise, its financial structure (including its liquidity and solvency) and its ability to affect the amounts and timings of cash flows in order to adapt to changing circumstances and opportunities.
- Cash flow information is useful in assessing the ability of the enterprise to generate cash and cash equivalents and enables users to develop models to assess and compare the present value of the future cash flows of different enterprises.
- It also enhances the comparability of the reporting of operating performance by different enterprises because it eliminates the effects of using different accounting treatments for the same transactions and events.
- Historical cash flow information is often used as an indicator of the amount, timing and certainty of future cash flows. It is also helpful in checking the accuracy of past assessments of future cash flows and in

examining the relationship between profitability and net cash flow and impact of changing prices.

6.3 Cash and Cash Equivalents

As stated earlier, cash flow statement shows inflows and outflows of cash and cash equivalents from various activities of an enterprise during a particular period. As per AS-3, 'Cash' comprises cash in hand and demand deposits with banks, and 'Cash equivalents' means short-term highly liquid investments that are readily convertible into known amounts *of cash and which are subj*ect to an insignificant risk of changes in value. Thus, cash equivalents refer to such investments that are held for the purpose of meeting short-term cash commitments rather than for investments or other purposes. An investment normally qualifies as cash equivalent only when it has a short maturity, of say, three months or less from the date of acquisition. Investments in shares are excluded from cash equivalents unless they are in substantial cash equivalents. For example, preference shares of a company acquired shortly before their specific redemption date, provided there is only insignificant risk of failure of the company to repay the amount at maturity. Similarly, short-term marketable securities which can be readily converted into cash are treated as cash equivalents.

6.4 Cash Flows

'Cash Flows' implies movement of cash in and out of non-cash items. Receipt of cash from a non-cash item is termed as cash inflow while cash payment in respect of such items as cash outflow. For example, purchase of machinery by paying cash is cash outflow while sale proceeds received from sale of machinery is cash inflow. Other examples of cash flows include collection of cash from debtors, payment to creditors, payment to employees, receipt of dividend, interest payments, etc.

As per AS 3, cash flows exclude movements between items that constitute cash or cash equivalents because these components are part of the cash management of an enterprise rather than part of its operating, investing of financing activities. Cash management includes the investment of excess cash in cash equivalents. Hence, purchase of marketable securities or short-term investment which constitutes cash equivalents is not considered while preparing cash flow statement.

6.5 Classification of Activities for the Preparation of Cash Flow Statement

You know that various activities of an enterprise result into cash flows (inflows or receipts and outflows or payments) which is the subject matter of a cash flow statement. As per AS-3, these activities are to be classified into three categories: (1) operating, (2) investing, and (3) financing activities so as to show separately the cash flows generated (or used) by (in) these activities. This helps the users of cash flow statement to assess the impact of these activities on the financial position of an enterprise and so also on its cash and cash equivalents.

6.5.1 Cash from Operating Activities

As per AS-3, operating activities are the activities that constitute the primary or main activities of an enterprise, for example, for a company manufacturing garments, procurement of raw material, incurrence of manufacturing expenses, sale of garments, etc. These are the principal revenue producing activities (or the main activities) of the enterprise and other activities that are not investing or financing activities. The amount of cash from operations' indicate the internal solvency level of the company, and is regarded as the key indicator of the extent to which the operations of the enterprise have generated sufficient cash flows to maintain the operating capability of the enterprise, paying dividends, making of new investments and repaying of loans without recourse to external source of financing. Information about the specific components of historical operating cash flows is useful in conjunction with other information, in forecasting future operating cash flows.

Cash flows from operating activities are primarily derived from the main activities of the enterprise. Therefore, they generally result from the transactions and other events that enter into the determination of net profit or loss. Examples of cash flows from operating activities are:

Cash Inflows from operating activities

- cash receipts from sale of goods and the rendering of services.
- cash receipts from royalties, fees, commissions and other revenues.

Cash Outflows from operating activities

- Cash payments to suppliers for goods and services.
- Cash payments to and on behalf of the employees.
- Cash payments to an insurance enterprise for premiums and claims, annuities, and other policy benefits.
- Cash payments or refunds of income taxes unless they can be specifically identified with financing and investing activities.

  The net position is shown in case of operating cash flows.

Some transactions such as sale of an item of plant may give rise to a gain or loss which is included in the determination of net profit or loss. However, the cash flows relating to such transactions are cash flows from investing activities which are discussed in detail later.

An enterprise may hold securities and loans for dealing or trading purposes in which case they are similar to inventory acquired specifically for resale. Therefore, cash flows arising from the purchase and sale of dealing or trading securities are classified as operating activities. Similarly, cash advances and loans made by financial enterprises are usually classified as operating activities since they relate to main activity of that enterprise.

6.5.2 Cash from Investing Activities

Investing activities relate to purchase and sale of long-term assets or fixed assets such as machinery, furniture, land and building, etc. Transactions related to long-term investment are also investing activities. As per AS-3, investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

Separate disclosure of cash flows from investing activities is important because they represent the extent to which expenditures have been made for resources intended to generate future income and cash flows. Examples of cash flows arising from investing activities are:

Cash Outflows from investing activities

- Cash payments to acquire fixed assets including intangibles and capitalised research and development.
- Cash payments to acquire shares warrants or debt instruments of other enterprises other than the instruments considered to be cash equivalents or held for trading purposes.
- Cash advances and loans made to third party (other than advances and loans made by a financial enterprise wherein it is operating activities).

Cash Inflows from Investing Activities

- Cash receipt from disposal of fixed assets including intangibles.
- Cash receipt from the repayment of advances or loans made to third parties (except in case of financial enterprise).
- Cash receipt from disposal of shares, warrants or debt instruments of other enterprises other than receipts from those instruments considered to be cash or cash equivalents or held for trading purposes.
- Interest received in cash from loans and advances.
- Dividend received from investments in other enterprises.

6.5.3 Cash from Financing Activities

As the name suggests, financing activities relate to long-term funds or capital of an enterprise, e.g. cash proceeds from issue of equity shares, debentures, raising long-term bank loans, redemption of bank loan, etc. As per AS-3, financing activities are activities that result in changes in the size and composition of the owners' capital (including preference share capital in case of a company) and borrowings of the enterprise. Separate disclosure of cash flows arising from financing activities is important because it is useful in predicting claims on future cash flows by providers of funds (both capital and borrowings) to the enterprise. Examples of financing activities are:

Cash Inflows from financing activities

- Cash proceeds from issuing shares or other similar instruments.
- Cash proceeds from issuing debentures, loans, bonds and other short or long-term borrowings.

Cash Outflows from financing activities

- Cash repayments of amounts borrowed.
- Interest paid on loans, debentures and advances.
- Dividends paid on equity and preference capital.

It is important to mention here that a transaction may include cash flows that are classified differently. For example, when the instalment paid in respect of a fixed asset acquired on deferred payment basis includes both interest and loan, the interest element is classified under financing activities and the loan element is classified under investing activities. Moreover, same activity may be classified differently for different enterprises. For example, purchase of shares is an operating activity for a share brokerage firm while it is investing activity in case of other enterprises.

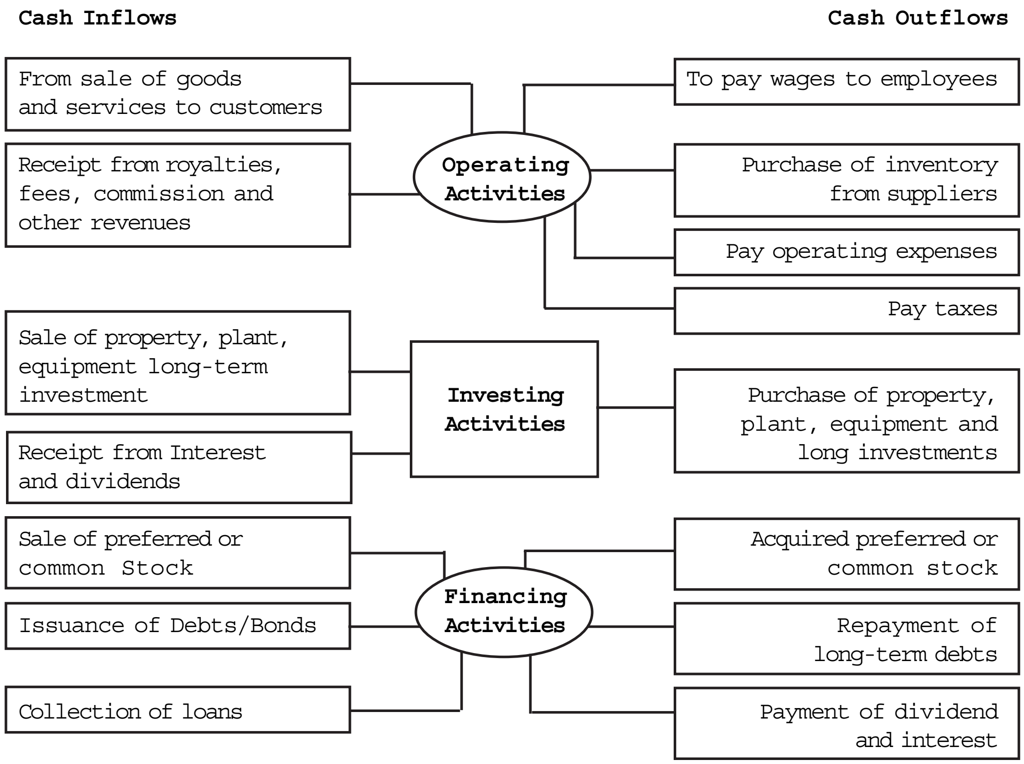

Fig. 6.1: *Classification of Cash inflows and Cash Outflows Activities*

6.5.4 Treatment of Some Peculiar Items

Extraordinary items

Extraordinary items are not the regular phenomenon, e.g. loss due to theft or earthquake or flood. Extraordinary items are non-recurring in nature and hence cash flows associated with extraordinary items should be classified and disclosed separately as arising from operating, investing or financing activities. This is done to enable users to understand their nature and effect on the present and future cash flows of an enterprise.

Interest and Dividend

In case of a financial enterprise (whose main business is lending and borrowing), interest paid, interest received and dividend received are classified as operating activities while dividend paid is the financing activity.
In case of a non-financial enterprise, as per AS-3, it is considered more

appropriate that payment of interest and dividend paid are classified as financing activities whereas receipt of interest and dividends are classified as investing activities.

Taxes on Income and Gains

Taxes may be income tax (tax in normal profit), capital gains tax (tax on capital profits), dividend tax (tax on the amount distributed as dividend to share holders). AS 3 requires that cash flows arising from taxes on income should be separately disclosed and should be classified as cash flows from operating activities unless they can be specifically identified with financing and investing activities. This clearly implies that:

- tax on operating profit should be classified as operating cash flows.
- dividend tax, i.e. tax paid on dividend should be classified as financing activity along with dividend paid.
- Capital gains tax paid on sale of fixed assets should be classified under investing activities.

Non-cash Transactions

As per AS-3, investing and financing transactions that do not require the use of cash or cash equivalents should be excluded from a cash flow statement. Examples of such transactions are – acquisition of machinery by issue of equity shares, or redemption of debentures by issue of equity shares. Such transactions should be disclosed elsewhere in the financial statements in a way that provide all the relevant information about these investing and financing activities. Hence, stocks acquired by issue of shares are not disclosed in cash flow statement.

With these three classifications, Cash Flow Statement is shown in Figure 6.1.

Cash Flow Statement
(Main heads only)

(A) Cash flows from operating activities	xxx
(B) Cash flows from investing activities	xxx
(C) Cash flows from financing activities	xxx
Net increase (decrease) in cash and cash equivalents (A + B + C)	xxx
+ Cash and cash equivalents at the beginning	xxx
= Cash and cash equivalents at the end	xxxx

Fig. 6.1 : *Sharing Specimen Cash Flow Statement*

Test your Understanding - I

Classify the following activities into operating activities, investing activities, financing activities, cash activities.

1.	Purchase of machinery.	2.	Proceeds from issuance of equity share capital.
3.	Cash Sales.	4.	Proceeds from long-term borrowings.
5.	Proceeds from sales of old machinery.	6.	Cash receipt from debtors.
7.	Trading commission received.	8.	Purchase of investment.
9.	Redemption of preference shares.	10.	Cash purchase.
11.	Proceeds from sale of investment.	12.	Purchase of goodwill.
13.	Cash paid to supplier.	14.	Interim dividend paid on equity shares.
15.	Wages and salaries paid.	16.	Proceeds from sale of patents.
17.	Interest received on debentrues held as investments.	18.	Interest paid on long-term borrowings.
19.	Office and administrative expenses paid.	20.	Manufacturing overhead paid.
21.	Dividend received on shares held as investment.	22.	Rent received on property held as investment.
23.	Selling and distribution expenses paid.	24.	Income tax paid.
25.	Dividend paid on preferences shares.	26.	Underwriting commission paid.
27.	Rent paid.	28.	Brokerage paid on purchase of investment.
29.	Bank overdraft.		
30.	Cash credit.	31.	Short-term deposit.
32.	Marketable securities.	33.	Refund of income-tax received.

6.6 Ascertaining Cash Flow from Operating Activities

Operating activities are the main source of revenue and expenditure in an enterprise. Not only that, this aspect is most complex and regarded as the major problem area faced while preparing the cash flow statement. Therefore, the ascertainment of cash flows from operating activities need special attention.

As per AS-3, an enterprise should report cash flows from operating activities using either by using :

- Direct method whereby major classes of gross cash receipts and gross cash payments are disclosed;

or

- Indirect method whereby net profit or loss is duly adjusted for the effects of (1) transactions of a non-cash nature, (2) any deferrals or accruals of past/future operating cash receipts, and (3) items of income or expenses associated with investing or financing cash flows. It is important to mention here that under indirect method, the starting point is net profit/ loss before taxation and extra ordinary items as per Income Statement of the enterprise. Then this amount is for non-cash items, etc. adjusted for ascertaining cash flows from operating activities.

Accordingly, cash flow from operating activities can be determined using either the Direct method or the Indirect method. These methods are discussed in detail as follows.

6.6.1 Direct Method

As the name suggests, under direct method, major heads of cash inflows and outflows (such as cash received from debtors, salary payments, etc) are considered.

It is important to note here that items are recorded on accrual basis in Profit and Loss Account. Hence, certain adjustments are made to convert them into cash basis such as the following :

1. Cash receipts from customers = Sales+ Debtors and Bills Receivable in the beginning – Debtors and Bills Receivable in the end.
2. Cash payments to suppliers = Purchases + Creditors and Bills Payable in the beginning – Creditors and Bills Payable in the end.
3. Purchases = Cost of Goods Sold – Opening Stock + Closing Stock
4. Cash Expenses = Expenses on Accrual basis – Prepaid Expenses in the beginning and Outstanding Expenses in the end + Prepaid Expenses in the end and Outstanding Expenses in the beginning.

However, the following items are not to be considered:

1. Non-cash items such as depreciation , discount on shares, etc. be written-off.
2. Items which are classified as investing or financing activities such as interest received, dividend paid, etc.

As per AS-3, under the direct method, information about major classes of gross cash receipts and cash payments may be obtained either–

- from the accounting records of the enterprise, or
- by adjusting sales cost of sales and other items in the statement of profit or loss for the following:
    - changes during the period in inventories and operating receivables and payables;
    - other non cash items; and
    - other items for which cash effects are investing or financing cash flows.

Figure 6.2 shows the Proforma of cash flows from operating activities using direct method.

Cash Flows from Operating Activities (Direct Method)

Cash flows from operating activities:		
Cash receipts from customers		xxx
(–)	Cash paid to suppliers and employees	xxx
=	Cash generated from operations	**xxx**
(–)	Income tax paid	xxx
=	Cash flow before extraordinary items	**xxx**
+/–	Extraordinary items	xxx
=	*Net cash from operating activities*	**xxxx**

Fig. 6.2 : *Proforma of Cash Flows from Operating Activities*

Illustration 1

From the following information, calculate cash flow from operating activities using direct method.

Profit and Loss Account
for the year ended on March 31, 2006

Dr. *Cr.*

Expenses/Losses	*Amount (Rs.)*	*Revenues/Gains*	*Amount (Rs.)*
Cost of Goods Sold	1,20,000	Sales	2,20,000
Gross Profit	1,00,000		
	2,20,000		**2,20,000**
Salary	30,000	Gross Profit	1,00,000
Insurance Premium	8,000		
Depreciation	20,000		
Income Tax	10,000		
Net Profit	32,000		
	1,00,000		**1,00,000**

Additional Information:

	April 01, 2005 (Rs.)	*March 31, 2006 (Rs.)*
Debtors	25,000	30,000
Bills Receivables	8,000	6,000
Creditors	17,000	15,000
Stock	22,000	27,000
Salaries Outstanding	2,000	3,000
Prepaid Insurance	5,000	5,500
Income Tax Outstanding	3,000	2,000

Solution

Cash Flows from Operating Activities	**(Rs.)**
Cash Receipts from Customers	2,17,000
Cash Paid to Suppliers	(1,27,000)
Cash Paid to Employees	(29,000)
Cash Paid for Insurance Premium	(8,500)
Cash generated from Operations	52,500
Income Tax Paid	(11,000)
Net Cash Inflow from Operations	**41,500**

Working Notes:

1. Cash Receipts from Customers is calculated as under :
   Cash Receipts from Customers = Sales+ Debtors and Bills Receivables in the beginning – Debtors and Bills Receivables in the end
   = Rs.2,20,000 + Rs.25,000 + Rs.8,000 – Rs.30,000 – Rs.6,000
   = Rs. 2,17,000
2. Purchases = Cost of Goods Sold – Opening Stock + Closing Stock
   = Rs. 1,20,000 – Rs. 22,000 + Rs. 27,000
   = Rs. 1,25,000
3. Cash Payments to Suppliers = Purchases+ Creditors and Bills Payables in the beginning – Creditors and Bills Payable in the end
   = Rs. 1,25,000 + Rs.17,000 – Rs.15,000
   = Rs. 1,27,000
4. Cash Expenses = Expenses on Accrual basis – Prepaid Expenses in the beginning and Outstanding Expenses in the end + Prepaid Expenses in the end and Outstanding Expenses in the beginning
5. Cash Paid to Employees = Rs. 30,000+Rs.2,000 – Rs.3,000
   = Rs. 29,000
6. Cash Paid for Insurance Premium = Rs. 8,000 – Rs.5,000+Rs.5,500
   = Rs. 8,500
7. Income Tax Paid = Rs. 10,000+Rs.3,000 – Rs.2,000
   = Rs. 11,000
8. It is important to note here that there are no extraordinary items.

6.6.2 Indirect Method

As mentioned earlier, indirect method of ascertaining cash flow from operating activities begins with the amount of net profit/loss. This is not so because income statement incorporates the effects of all operating activities of an enterprise. However, income statement is prepared on accrual basis (and not on cash basis). Moreover, it also includes certain non-operating items such as interest paid, profit/loss on sale of fixed assets, etc) and non-cash items (such as depreciation, goodwill to be written-off, etc. Therefore, it becomes necessary to adjust the amount of net profit/loss as shown by Profit and Loss Account for arriving at cash flows from operating activities. Let us look at the example :

Profit and Loss Account
for the year ended March 31, 2007

Dr. *Cr.*

Expenses/Losses	*Amount (Rs.)*	*Revenues/Gains*	*Amount (Rs.)*
Salaries	35,000	Gross Profit	1,00,000
Rent	15,000	Profit on Sale of Land	2,000
Depreciation	10,000		
Interest Paid	12,000		
Net Profit	30,000		
	1,02,000		1,02,000

The above Profit and Loss Account shows the amount of net profit of Rs.32,000. This has to be adjusted for arriving cash flows from operating activities. Let us take various items one by one.

1. *Depreciation* is a non-cash item and hence, Rs.10,000 charged as depreciation does not result in any cash flow. Therefore, this amount must be added back to the net profit.
2. *Interest paid* of Rs.12,000 is a cash outflow on account of financing activity. Therefore, this amount must also be added back to net profit while calculating cash flows from operating activities. This amount of interest will be shown as an outflow under the head of financing activities.
3. *Profit on sale of land* is cash inflow from investing activity. Hence, this amount must be deducted from the amount of net profit while calculating cash flows from operating activities.

The above example gives you an idea as to how various adjustments are made in the amount of net profit/loss. Other important adjustments relate to changes in working capital which are necessary (i.e. items of current assets and current liabilities) to convert net profit/loss which is based on accrual basis into cash flows from operating activities. Therefore, the increase in current assets and decrease in current liabilities are added to the net profit, and the decrease in current assets and increase in current liabilities are deducted from the net profit so as to arrive at the exact amount of net cash flow from operating activities. As per AS-3, under indirect method, net cash flow from operating activities is determined by adjusting net profit or loss for the effect of :

- Non-cash items such as depreciation, goodwill be written-off, provisions, deferred taxes, etc. which are to be added back.
- All other items for which the cash effects are investing or financing cash flows. The treatment of such items depend upon their nature. All investing and financing incomes are to be deducted from the amount of net profits while all such expenses are to be added back. For example, interest expense

which is a financing cash outflow is to be added back while interest income which is investing cash inflow is to be deducted from the amount of net profit.

- Changes in current assets and liabilities during the period. Increase in current assets and decrease in current liabilities are to be deducted while increase in current liabilities and decrease in current assets are to be added up.

Figure 6.3 shows the proforma of calculating cash flows from operating activities as per indirect method.

The direct method provides information which is useful in estimating future cash flows. But such information is not available under the indirect method. However, in practice, indirect method is mostly used by the companies for arriving at the net cash flow from operating activities.

Cash Flows from Operating Activities
(Indirect Method)

Net Profit/Loss before Tax and Extraordinary Items	
+ Deductions already made in Profit and Loss on account of Non-Cash items such as Depreciation, Goodwill to be Written-off.	xxx
+ Deductions already made in Profit and Loss on Account of Non-operating items such as Interest.	xxx
– Additions (incomes) made in Profit and Loss on Account of Non-operating Items such as Dividend Received, Profit on sale of Fixed Assets.	xxx
Operating Profit before Working Capital changes	
+ Increase in Current Liabilities	xxx
+ Decrease in Current Assets	xxx
– Increase in Current Assets	xxx
– Decrease in Current Liabilities	xxx
Cash Flows from Operating Activities before Tax and Extraordinary Items.	
– Income Tax Paid	xxx
+/– Effects of Extraordinary Items	xxx
Net Cash from Operating Activities	**xxx**

Fig. 6.2: *Proforma of Cash Flows from Operating Activities (Indirect Method)*

As stated earlier, it may be noted that while working out the cash flow from operating activities, the starting point is the 'Net profit before tax and extraordinary items' and not the 'Net profit as per Profit and Loss Account', and that the income tax paid is deducted there from as the last item to arrive at the net cash flow from operating activities.

Illustration 2

Using the data given in Illustration 1, calculate cash flows from operating activities using indirect method.

Solution

Cash Flows from Operating Activities *(Rs.)*

	Net Profit before Taxation and Extraordinary Items (1)	42,000
	Adjustments for–	
+	Depreciation	20,000
=	Operating Profit before working capital changes	62,000
–	Increase in Sundry Debtors	(5,000)
+	decrease in Bills Receivables	+2,000
–	Increase in Inventories	(5,000)
–	Increase in Prepaid Insurance	(500)
–	Decrease in Sundry Creditors	(2,000)
+	Increase in Outstanding Salaries	+1,000
=	Cash generated from Operations	52,500
–	Income tax paid	(11,000)
=	*Net cash from Operating Activities*	**41,500**

You will notice that the amount of cash flows from operating activities are the same whether we use direct method or indirect method for its calculation.

Working Notes:

The net profit before taxation and extraordinary items has been worked out as under:

(1) Net Profit	=	Rs. 32,000
+ Income Tax provided for Profit and Loss	=	Rs.10,000
= Net Profit before Tax and Extraordinary Items	=	Rs.42,000

Illustration 3

Calculate cash flows from operating activities from the following information.

Profit and Loss Account for the year ended March 31, 2006

Expenses/Losses	*Amount (Rs.)*	*Revenues/Gains*	*Amount (Rs.)*
Rent	10,000	Gross Profit	50,000
Salary	25,000	Profit on Sale of Machinery	2,000
Depreciation	5,000	Income Tax Refund	3,000
Loss on Sale of Equipment	3,000		
Goodwill written-off	2,000		
Provision for Taxation	8,000		
Net Profit	2,000		
	55,000		**55,000**

Additional Information:

	April 01, 2005 Rs.	March 31, 2006 Rs.
Provision for Taxation	10,000	13,000
Outstanding Rent	2,000	2,500
Creditors	21,000	25,000
Debtors	15,000	21,000
Inventories	25,000	22,000

Solution

Cash Flows From Operating Activities

Net profit before taxation, and extraordinary items	10,000
Adjustments for:	
+ Depreciation	5,000
+ Loss on Sale of Equipment	3,000
+ Goodwill Written-off	2,000
– Profit on Sale of Machinery	(2,000)
– Income Tax Refund	(3,000)
Operating Profit before Working Capital charges	15,000
– Increase in Sundry Debtors	(6,000)
+ Decrease in Inventories	3,000
+ Increase in Sundry Creditors	4,000
+ Increase in Outstanding Rent	500
Cash generated from Operations	16,500
Income Tax Paid	(5,000)
Income Tax refund	3,000
Net Cash from Operating Activities	**14,500**

Working Notes:

1. Net profit before taxation & extraordinary item = Rs. 2,000+Rs.8,000 = Rs. 10,000
2. Income tax paid during the year has been ascertained by preparing provision for tax account as follows:

Provision for Taxation Account

Dr. *Cr.*

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Cash (Income tax paid during the year - Balancing Figure)		5,000	Balance b/d		10,000
			Profit and Loss		8,000
Balance c/d		13,000			
		18,000			**18,000**

Illustration 4

Charles Ltd. made a profit of Rs.1,00,000 after charging depreciation of Rs.20,000 on assets and a transfer to general reserve of Rs.30,000. The goodwill written-off was Rs.7,000 and gain on sale of machinery was Rs.3,000. Other information available to you (charges in the value of current assets and current liabilities) are debtors showed an increase of Rs,6,000; creditors an increase of Rs.10,000; prepaid expenses an increase of Rs.200; bills receivables a decrease of Rs.3,000; bills payables a decrease of Rs.4,000 and outstanding expenses a decrease of Rs. 2,000. Ascertain cash flow from operating activities.

Solution

	(Rs.)
Net Profit before Taxation	1,00,000
Adjustment for Non-cash and Non-operating Items :	
+ Depreciation	20,000
+ Transfer to general reserve	30,000
+ Goodwill written-off	7,000
– Gain on sale of machinery	(3,000)
Operating profit before working capital	1,54,000
Adjustment for working capital charges :	
– Increase in Debtors	(6,000)
+ Increase in Creditors	10,000
– Increase in Prepaid Expenses	(200)
+ Decrease in Bills Receivables	3,000
– Decrease in Bills Payables	(4,000)
– Decrease in Outstanding Expenses	(2,000)
= Net Cash from Operating Activities	1,54,800

Do it Yourself

1. The Profit and Loss Account of Raj Limited is given here under:

Profit and Loss Account
for the year ended March 31, 2007

Dr. *Cr.*

Expenses/Losses		*Amount (Rs.)*	*Revenues/Gains*		*Amount (Rs.)*
Opening Stock		2,00,000		Sales:	
Purchases:			Cash Sales	8,00,000	
Cash Purchases	4,00,000		Credit Sales	34,00,000	
Credit Purchases	17,00,000		*Less* Returns	(2,00,000)	
Less Returns	(1,00,000)		Net Sales		40,00,000
Net Purchases		20,00,000			
Administrative Expenses		10,20,000	Trading Commission		20,40,000
Discount Allowed to Customers		1,20,000	Discount Recd. from Suppliers		60,000
Bad Debts		1,00,000	Closing Stock		1,00,000
Depreciation		3,80,000			
Provision for Tax		8,00,000			
Net Profit		15,80,000			
		62,00,000			**62,00,000**

Additional Information:

	(Rs.)	(Rs.)
Bills Receivable	20,00,000	40,00,000
Bills Payable	20,00,000	10,00,000
Outstanding Administrative Expenses	10,000	20,000
Prepaid Administrative Expenses	20,000	10,000
Accrued Trading Expenses	20,000	40,000
Advance Trading Expenses	40,000	20,000
Provision for Taxation	10,00,000	12,00,000

Ascertain Cash from Operations. Show your workings clearly.

2. From the following information calculate net cash from operations:

Particulars	(Rs.)
Operating Profit after Provision for Tax of Rs. 1,53,000.	6,28,000
Insurance proceeds from the famine settlement	1,00,000

Proposed Dividend for the current year	72,000
Depreciation	1,40,000
Loss on Sale of Machinery	30,000
Profit on Sale of Investment	20,000
Dividend Received on Investments	6,000
Decrease in Current Assets (other than cash and cash equivalents)	10,000
Increase in Current Liabilities	1,51,000
Increase in Current Assets other than Cash and Cash Equivalents	6,00,000
Decrease in Current Liabilities	64,000
Income Tax Paid	1,18,000
Refund of Income Tax Received	3,000

Test your Understanding – II

1. Choose one of the two alternatives given below and fill in the blanks in the following statements:

(a) If the net profits earned during the year is Rs. 50,000 and the amount of debtors in the beginning and the end of the year is Rs. 10,000 and Rs. 20,000 respectively, then the cash from operating activities will be equal to Rs. ________________ (Rs. 40,000/Rs. 60,000)

(b) If the net profits made during the year are Rs. 50,000 and the bills receivables have decreased by Rs. 10,000 during the year then the cash flow from operating activities will be equal to Rs. ______________ (40,000/ Rs. 60,000)

(c) Expenses paid in advance at the end of the year are _______________ the profit made during the year (added to/deducted from).

(d) An increase in accrued income during the particular year is ______________ the net profit (added to/deducted from).

(e) Goodwill written-off is _______________ the profit made during the year for calculating the cash flow from operating activities (added to/ deducted from)

(f) For calculating cash flow from operating activities, provision for doubtful debts is ________________ the profit made during the year (added to/ deducted from).

2. While computing cash from operating activities, indicated whether the following items will be added or subtracted from the net profit- if not to be considered write NC

	Items	Result
(a)	Increase in the value of creditors	
(b)	Increase in the value of patents	
(c)	Decrease in prepaid expenses	
(d)	Decrease in income received in advance	
(e)	Decrease in value of stock	
(f)	Increase in share capital	
(g)	Increase in the value of bills receivables	
(h)	Increase in the amount of outstanding expenses	
(i)	Conversion of debentures into shares	
(j)	Decrease in the value of bills payables	
(k)	Increase in the value of debtors	
(l)	Decrease in the amount of accrued income.	

Sometimes, neither the amount of net profit is specified nor the Profit and Loss Account is given. In such a situation, the amount of net profit can be worked out by comparing the Profit, and Loss Account balance given in the comparative Balance Sheets for two years. The difference is treated as the net profit for the year; and, then, by adjusting it with the amount of provision for tax made during the year (as worked out by comparing the provision for tax balances of two years given in balance sheets), the amount of 'Net Profit before tax' can be ascertained (see Illustration (see Illustration 7 and 8)

6.7 Ascertainment of Cash Flow from Investing and Financing Activities

The details of item leading inflows and outflows from investing and financing activities have already been outlined. While preparing the cash flow statement, all major items of gross cash receipts, gross cash payments, and net cash flows from investing and financing activities must be shown separately under the headings 'Cash Flow from Investing Activities' and 'Cash Flow from Financing Activities' respectively.'

The ascertainment of net cash flows from investing and financing activities have been briefly dealt with in Illustrations 5 and 6.

Illustration 5

Welprint Ltd. has given you the following information:

	(Rs.)
Machinery as on April 01, 2004	50,000
Machinery as on March 31, 2005	60,000
Accumulated Depreciation on April 01, 2004	15,000
Accumulated Depreciation on March 31, 2005	25,000

During the year, a Machine costing Rs. 25,000 with Accumulated Depreciation of Rs. 15,000 was sold for Rs. 13,000.

Calculate cash flow from Investing Activities on the basis of the above information.

Solution

Cash Flows from Investing Activities	*(Rs.)*
Sale of Machinery	13,000
Purchase of Machinery	(35,000)
Net cash used in Investing Activities	(22,000)

Working Notes:

Machinery Account

Dr. Cr.

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Balance b/d		50,000	Cash (proceeds from sale of machine)		13,000
Profit and Loss (profit on sale of machine		3,000	Accumulated Depreciation		15,000
Cash (balancing figure–new machinery purchased)		35,000	Balance c/d		60,000
		88,000			**88,000**

Accumulated Depreciation Account

Dr. Cr.

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Machinery		15,000	Balance b/d		25,000
Balance c/d		15,000	Profit and Loss (Depreciation provided during the year)		5,000
		30,000			**30,000**

Illustration 6

From the following information, calculate cash flows from financing activities:

	(Rs.)	*(Rs.)*
Long-term Loans	2,00,000	2,50,000

During the year, the company repaid a loan of Rs. 1,00,000.

Solution

Cash flows from Financing Activities	
Proceeds from long-term borrowings	1,50,000
Repayment of long-term borrowings	(1,00,000)
Net cash inflow from Financing Activities	*50,000*

Working Notes:

Long-term Loan Account

Dr. *Cr.*

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Cash (loan repaid)		1,00,000	Balance b/d		2,00,000
Balance c/d		2,50,000	Cash (new loan raised)		1,50,000
		3,50,000			**3,50,000**

Do it Yourself

1. From the following particulars, calculate cash flows from investing activities:

	Purchased (Rs.)	*Sold* (Rs.)
Plant	4,40,000	50,000
Investments	1,80,000	1,00,000
Goodwill	2,00,000	
Patents		1,00,000

Interest received on debentures held as investment Rs. 60,000

Dividend received on shares held as investment Rs. 10,000

A plot of land had been purchased for investment purposes and was let out for commercial use and rent received Rs. 30,000.

2. From the following Information, calculate cash flows from investing and financing activities:-

	2005	*2006*
Machine at cost	5,00,000	9,00,000
Accumulated Deprciation	3,00,000	4,50,000
Equity Shares Capital	28,00,000	35,00,000
Bank Loan	12,50,000	7,50,000

In year 2006, machine costing Rs.2,00,000 was sold at a profit of Rs.1,50,000, Depreciation charged on machine during the year 2006 amounted to Rs.2,50,000.

6.8 Preparation of Cash Flow Statement

As stated earlier cash flow statement provides information about change in the position of Cash and Cash Equivalents of an enterprise, over an accounting period. The activities contributing this change are classified into operating, investing and financial. The methology of working out the net cash flow (or use) from all the three activities for an accounting period has been explained in details and a brief format of Cash Flow Statement has also been given in Fig. 6.1. However, while preparing a cash flow statement, full details of inflows and outflows are given under head including the net cash flow (or use) arise there from. The aggregate of the net cash flows (or use) is worked out and is shown as, Net Increase Decrease in cash and Cash Equivalents' to which the amount of 'cash and cash equivalent at the beginning' is added and thus the amount of 'cash and cash equivalents at the end' is arrived at as shown in Fig. 6.1. This figure will be the same as the total amount of cash in hand, cash at bank (or overdraft) and cash equivalants (if any) given in the balance sheet (see Illustrations 7 to 10). Another point that needs to be noted is that when cash flows from operating activities are worked out by an indirect method and shown as such in the cash flow statement, the statement itself is termed as 'Indirect method cash flow statement'. Thus, the cash flow statements prepared in Illustrations 7, 8 and 9 fall under this category as the cash flows from operating activities have been worked out by indirect method. Similarly, if the cash flows from operating activities are worked by direct method while preparing the cash flow statement, it will be termed as 'direct method Cash Flow Statement'. Illustration 10 shows both types of Cash Flow Statement. However, unless it is specified clearly as to which method is to be used, the cash flow statement may preferably be prepared by an indirect method as is done by most companies in practive. Look at these flow statements of Grase in Industries, Ucal Fuel Systems and Sterlite optical Technologies given at the end of the Chapter.

Illustration 7

From the following information, prepare Cash Flow Statement for Pioneer Ltd.

Balance Sheet of Pioneer Ltd. as on March 31, 2005

Liabilities	*March 31, 2004*	*March 31, 2005*	*Assets*	*March 31, 2004*	*March 31, 2005*
Equity Shares	5,00,000	7,00,000	Patents	1,00,000	95,000
Profit and Loss	2,00,000	3,50,000	Equipments	2,00,000	2,30,000
Bank Loan	1,00,000	50,000	Furniture	3,00,000	2,70,000
Proposed Dividend	50,000	70,000	Investments	-----	1,00,000
Provison of Taxation	30,000	50,000	Debtors	80,000	1,20,000
Creditors	50,000	45,000	Store	50,000	1,30,000
Oustanding Rent	5,000	7,000	Cash	5,000	27,000
			Bank	2,00,000	3,00,000
	9,35,000	**12,72,000**		**9,35,000**	**12,72,000**

During the year, equipment costing Rs.80,000 was purchased. Loss on sale of equipment amounted to Rs.5,000. Depreciation of Rs.15,000 and Rs. 3,000 were provided for equipments and furniture.

Solution

Cash Flow Statement

		(Rs.)
I	Cash flows from Operating Activities :	
	Net profit before taxation & extraordinary items	2,00,000
	Provision for :	
	Depreciation on Equipment	15,000
	Depreciation on Furniture	30,000
	Patents Written-off	5,000
	Proposed Dividend	70,000
	Loss on Sale of Equipment	5,000
	Operating Profit before Working Capital Charges	3,25,000
	– Decrease in Creditors	(5,000)
	+ Increase in Outstanding Rent	2,000
	– Increase in Debtors	(40,000)
	– Increase in Goods	(80,000)
	as generated from Operating Activities	
		2,02,000
	(–) Tax Paid	(30,000)
A.	Cash Inflows from Operating Activities	1,72,000

II.	Cash flows from Investing Activities:	
	Proceeds from Sale of Equipments	30,000
	Purchase of new Equipment	(80,000)
	Purchase of Investments	(1,00,000)
B.	Cash used in Investing Activities	(1,50,000)
III.	Cash flows from Financing Activities:	
	Issues of Equity share capital	2,00,000
	Repayment of bank loan	(50,000)
	Payment of Dividend	(50,000)
C.	Cash Inflows from Financing Activities	1,00,000
	Net increase in Cash & Cash Equivalents (A+B+C)	1,22,000
	+ Cash and Cash Equivalents in the beginning	2,05,000
	Cash and Cash Equivalents in the end	3,27,000

Working Notes:

(1)

Equipment Account

Dr. *Cr.*

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Balance b/d		2,00,000	Depreciation (balancing figure)		15,000
Cash		80,000	Bank		30,000
			Profit & Loss (Loss on sale)		5,000
			Balance c/d		2,30,000
		2,80,000			**2,80,000**

(2) Patents of Rs. 5,000 (i.e. Rs.1,00,000 – Rs. 95,000) were written-off during the year, and depreciation on furniture Rs. 30,000. (Rs. 3,00,000 – Rs. 2,70,000)

(3) It is assumed that dividend of Rs.50,000 and tax of Rs.30,000 provided in 2003-2004 has been paid during the year 2004-05. Hence, proposed dividend and provision for tax during the year amounts to Rs.70,000 and Rs. 50,000 respectively.

		(Rs.)
(4)	Profit and Loss at the end	3,50,000
	(–) Profit and Loss in the beginning	2,00,000
(5)	Net Profit during the year	1,50,000
	+ Provision for Tax during the year	50,000
	Net Profit before Taxation & Extraordinary Items	2,00,000

Illustration 8

From the following information, prepare a Cash Flow Statement for Xerox Limited.

Balance Sheet of Xerox Ltd. as on March 31, 2007

Liabilities	*March 31,2006*	*March 31,2007*	*Assets*	*March 31,2006*	*March 31,2007*
Equity Share	10,00,000	15,00,000	Goodwill	2,00,000	1,80,000
Profit and Loss	6,00,000	7,50,000	Land & Building	8,00,000	6,50,000
Debentures	2,00,000	–	Plant & Machinery	4,00,000	3,60,000
Bank Loan	–	1,00,000	Investments	–	6,00,000
Profit for Taxation	80,000	95,000	Debtors	1,50,000	2,00,000
Creditors	60,000	70,000	Stock	1,00,000	1,80,000
	50,000	30,000	Cash	50,000	70,000
			Bank	2,90,000	3,05,000
	19,90,000	**25,45,000**		**19,90,000**	**25,45,000**

Dividend of Rs.1,50,000 was proposed and paid during the year. Income tax paid during the year includes Rs.15,000 on account of Dividend Tax. Moreover, during the year, Land and Building worth Rs.1,50,000 was sold at a profit of 10%. The rate of Depreciation on Plant and Machinery is 10%.

Solution

Cash Flow Statement

		(Rs.)
I	Cash flows from Operating Activities	
	Net Profit before Taxation and Extraordinary Items	2,45,000
	Adjustment for –	
	+ Depreciation	40,000
	+ Goodwill written-off	20,000
	+ Proposed Dividend	1,50,000
	– Profit on Sale of Land	(15,000)
	= Operating Profit before working capital charges	4,40,000
	+ Increase in Creditors	10,000
	– Decrease in Bills Paybles	(20,000)
	– Increase in Debtors	(50,000)
	– Increase in Stock	(80,000)
	= Cash generated from Operations	3,00,000
	– Income Tax Paid (1)	(65,000)
	A. Cash Inflows from Operations	2,35,000

II.	Cash flows from Investing Activities		
		Proceeds from Sale of Land and Building	1,65,000
		Purchase of Investment	6,00,000
	B.	Cash used in Investing Activities	(4,35,000)
III.	Cash flows from Financing Activities		
		Proceeds from issue of Equity Share Capital	5,00,000
		Redemption of Debentures	(2,00,000)
		Proceeds from raising Bank Loan	1,00,000
		Dividend Paid	(1,50,000)
		Dividend Tax Paid	(15,000)
	C.	Cash flows from Financing Activities	2,35,000
		Net Increase in cash and cash equivalents (A+B+C)	35,000
		+ Cash and Cash Equivalents in the beginning	3,40,000
		Cash and Cash Equivalent at the end	3,75,000

Working Notes:

(1) Total income tax paid during the year Rs. 80,0000
(-) Dividend tax paid (given) Rs. (15,000)

Income tax paid for operating activities Rs. 65,000

(2) Net profit earned during the year after tax and dividend
= Rs. 7,50,000 – 6,00,000 = Rs.1,50,000

(3) Net profit before tax
= Rs. 1,50,000 + Provision for tax made
= Rs. 1,50,000 + 95,000 (See provision for taxation account)
= Rs. 2,45,000

Equity Share Capital Account

Dr. *Cr.*

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Balance c/d		15,00,000	Balance b/d		10,00,000
			Cash (New capital raised)		5,00,000
		15,00,000			**15,00,000**

Debenture Account

Dr. *Cr.*

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Cash (Redemption)		20,000	Balance b/d		20,000
		20,000			**20,000**

Bank Account

Dr. Cr.

Particulars	J.F.	Amount (Rs.)	Particulars	J.F.	Amount (Rs.)
Balance c/d		1,00,000	Cash		1,00,000
		1,00,000			**1,00,000**

Provision for Taxation Account

Dr. Cr.

Particulars	J.F.	Amount (Rs.)	Particulars	J.F.	Amount (Rs.)
Cash (Tax paid- which includes Rs. 15,000 as dividend		80,000	Balance b/d		80,000
			Profit and Loss (Provision made during the year)		95,000
Balance c/d		95,000			
		1,75,000			**1,75,000**

Land and Building Account

Dr. Cr.

Particulars	J.F.	Amount (Rs.)	Particulars	J.F.	Amount (Rs.)
Balance b/d		8,00,000	Cash		1,65,000
Profit and Loss (Profit on sale)		15,000	Balance c/d		6,50,000
		8,15,000			**8,15,000**

Proposed Dividend Account

Dr. Cr.

Particulars	J.F.	Amount (Rs.)	Particulars	J.F.	Amount (Rs.)
Cash		1,50,000	Profit and Loss		1,50,000
		1,50,000			**1,50,000**

Plant and Machinery Account

Dr. Cr.

Particulars	J.F.	Amount (Rs.)	Particulars	J.F.	Amount (Rs.)
Balance b/d		4,00,000	Depreciation		40,000
					3,60,000
		4,00,000			**4,00,000**

Illustration 9

From the following particulars related to Oswal Agro Mills Ltd., prepare cash Flow Statement for the year ended on March 31, 2006

Particulars	**31.3.06**	**31.03.05**
Source of funds	(Rs. lakh)	(Rs. Lakh)
Shareholders funds		
Capital	1,300	1,400
Reserve and Surplus	4,700	4,000
Grand Total	**6,000**	**5,400**
Application of funds		
Fixed Assets		
Gross Block	**3,600**	**3,400**
(-) Depreciation	(1,200)	(1,000)
Net Block	**2,400**	**2,400**
Investments	300	200
Current Assets		
- Inventories	1,200	1,300
- Sundry Debtors	800	900
- Cash and Bank Balance	1,200	800
- Loans and Advances	800	800
Total		
Less : Current Liabilities		
- Trade Creditors	500	400
- Short term loans	200	600
Total	(700)	(1,000)
Net Current Assets	3,300	2,800
Gross Total	6,000	5,400

Income Statement for the year ended on March 31, 2006
(Rs. in lakh)

Sales	2,800
Other income (Dividend income)	1,000
(–) Expenditure	3,800
Labour cost	(600)
Interest paid	(200)
Depreciation	(200)
Profit before Tax	2,800
(–) Tax Paid	(1,000)
(–) Loss due to earthquake	(1,100)
Net Profit	700

You are given that no dividends were paid by the company during the year 2006. Out of fixed assets, lands worth Rs.1,000 having no accumulated depreciation were sold at no profit or no loss.

Solution

Cash Flow Statement

Cash Flows from Operating Activities	
Net Profit before Tax and Extraordinary Items (1)	2,800
Adjustment for :	
+ Interest paid	200
+ Depreciation	200
Operating profit before working capital charges	3,200
Adjustment for :	
+ Decrease in Inventories	100
+ Decrease in Sundry Debtors	100
+ Increase in Sundry Creditors	100
– Decrease in Short Term Loans	(400)
Cash generated from Operations	3,100
(-) Income Tax Paid	(1,000)
(-) Loss due to earthquake	(1,100)
A. Net cash from Operating Activities	1,000
Cash flows from Investing Activities	
Sale of Land (2)	1,000
Purchase of Fixed Assets (2)	(1,200)
Purchase of Investments	(100)
B. Net cash	(300)
Cash flows from Financing Activities	
Interest Paid	(200)
Redemption of Capital	(100)
	(300)
C. Net Cash used in Financing Activities	
Net increase in Cash and Cash Equivalents during the year (A+B+C)	400
+ Cash and Cash Equivalents in the beginning of the year	800
= Cash and Cash Equivalents in the end	**1,200**

Working Notes:

(Rs. in lakh)

(1) Net Profit before Tax and Extraordinary Items = Rs. 700 + Rs.1,100 + Rs.1,000
= Rs. 2,800

(2) **Fixed Assets Account**

Dr. Cr.

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Balance b/d		3,400	Cash (Sale of land)		1,000
Cash (Purchase of fixed assets)		1,200	Balance c/d		3,600
		4,600			**4,600**

Accumulated Depreciation Account

Dr. Cr.

Particulars	*J.F.*	*Amount (Rs.)*	*Particulars*	*J.F.*	*Amount (Rs.)*
Balance c/d		1,200	Balance b/d		1,000
			Profit and Loss		200
		1,200			**1,200**

Illustration 10

From the following information, prepare a Cash Flow Statement as per AS-3 for Banjara Ltd, using both direct and indirect methods.

Balance Sheet as on March 31, 2006

(Rs.'000)

	2006	2005
Assets		
Cash on Hand and balances with Bank	200	25
Marketable Securities (having one month maturity)	670	135
Sundry Debtors	1,700	1,200
Interest Receivable	100	-
Inventories	900	1,950
Investments	2,500	2,500
Fixed Assets at cost	2,180	1,910

Accumulated Depreciation	(1,450)	(1,060)
Fixed Assets (net)	730	850
Total Assets	**6,800**	**6,660**
Liabilities		
Sundry Creditors	150	1,890
Interest Payable	230	100
Income Tax Payable	400	1,000
Long-term Debt	1,110	1,040
Total liabilities	**1,890**	**4,030**
Shareholders' Fund		
Share Capital	1,500	1,250
Reserves	3,410	1,380
Total shareholders' Fund	**4,910**	**2,630**
Total Liabilities and Shareholders' Fund	**6,800**	**6,660**

Statement of Profit or Loss for the year ended March 31, 2006

	(Rs.'000)
Sales	30,650
Cost of sales	(26,000)
Gross profit	4,650
Depreciation	(450)
Administrative and selling expenses	(910)
Interest expense	(400)
Interest income	300
Dividend income	200
Net profit before taxation and extraordinary items	3,390
Extraordinary items:	
Insurance proceeds from earthquake disaster settlement	140
Net profit after Extraordinary Items	3,530
Income tax	(300)
Net Profit	3,230

Additional Information: (Rs.'000)

a. An amount of Rs. 250 was raised from the issue of share capital and a further Rs. 250 was raised from long-term borrowings.

b. Interest expense was Rs. 400 of which Rs. 170 was paid during the period. Rs. 100 relating to interest expense of the prior period was also paid during the period.

c. Dividends paid were Rs. 1,200.

d. Tax deducted at source on dividends received (included in the tax expense of Rs. 300 for the year) amounted to Rs. 40.

e. During the period, the enterprise acquired Fixed Assets for Rs. 350. The payment was made in cash.

f. Plant with original cost of Rs. 80 and accumulated depreciation of Rs. 60 was sold for Rs. 20.

g. Sundry Debtors and Sundry Creditors include amounts relating to credit sales and credit purchases only.

Solution

Cash Flow Statement
(Direct Method)

(Rs.'000)

Cash Flows from Operating Activities		
Cash Receipts from Customers	30,150	
Cash Paid to Suppliers and Employees	(27,600)	
Cash generated from Operations	2,550	
Income Tax paid	(860)	
Cash Flow before Extraordinary Item	1,690	
Proceeds from earthquake disaster settlement	140	
Net Cash from Operating Activities		1,830
Cash Flows from Investing Activities		
Purchase of Fixed Assets	(350)	
Proceeds from Sale of Equipment	20	
Interest Received	200	
Dividends Received	160	
Net cash from Investing Activities		30
Cash Flows from Financing Activities		
Proceeds from issuance of Share Capital	250	
Proceeds from Long-term Borrowings	250	

Repayment of Long-term Borrowings	(180)	
Interest paid	(270)	
Dividends paid	(1,200)	
Net cash used in Financing Activities		(1,150)
Net increase in Cash and Cash Equivalents		710
Cash and cash equivalents at beginning of period		160
Cash and cash equivalents at end of period		870

Cash Flow Statement
(Indirect Method)

	(Rs.'000)
Cash Flows from Operating Activities	
Net Profit before Taxation and Extraordinary Item	3,390
Adjustments for:	
+ Depreciation	450
– Interest Income	(300)
– Dividend Income	(200)
+ Interest Expense	400
Operating Profit before working capital charges	3,740
Increase in Sundry Debtors	(500)
Decrease in Inventories	1,050
Decrease in Sundry Creditors	(1,740)
Cash generated from Operations	2,550
Income Tax paid	(860)
Cash flow before Extraordinary Items	1,690
Proceeds from earthquake disaster settlement	140
Net cash from Operating Activities	1,830
Cash Flows from Investing Activities	
Purchase of Fixed Assets	(350)
Proceeds from Sale of Equipment	20
Interest Received	200
Dividends Received (net of TDS)	160
Net cash from Investing Activities	30
Cash flows from Financing Activities	
Proceeds from issuance of Share Capital	250
Proceeds from Long-term Borrowings	250

Repayment of Long-term Borrowings	(180)
Interest Paid	(270)
Dividends Paid	(1,200)
Net Cash used in Financing Activities	(1,150)
Net Increase in Cash and Cash Equivalents	710
Cash and Cash Equivalents at the beginning of the period	160
Cash and Cash Equivalents at the end of the period	870

Working Notes:

(1) *Cash and Cash Equivalents*

Cash and Cash Equivalents consist of cash on hand and balances with banks, and investments in money-market instruments. Cash and Cash Equivalents included in the Cash Flow Statement comprise the following balance sheet amounts.

(Rs. '000)

	2006 *(Rs.)*	*2005* *(Rs.)*
Cash in Hand and balances with Bank	200	25
Short-term Investments	670	135
Cash and Cash Equivalents	870	160

(2) *Cash Receipts from Customers*

Sales	30,650
Add: Sundry Debtors at the beginning of the year	1,200
	31,850
Less : Sundry Debtors at the end of the year	1,700
	30,150

(3) *Cash paid to Suppliers and Employees*

Cost of Sales		26,000
Administrative and Selling Expenses		910
		26,910
Add: Sundry Creditors at the beginning of the year	1,890	
Inventories at the end of the year	900	2,790
		29,700
Less : Sundry Creditors at the end of the year	150	
Inventories at the beginning of the year	1,950	2,100
		27,600

(4) *Income Tax paid (including TDS from dividends received)* 300

Income Tax expense for the year

(including tax deducted at source from dividends received)

Add : Income Tax liability at the beginning of the year	1,000
	1,300
Less : Income Tax liability at the end of the year	400
	900

Out of Rs. 900, tax deducted at source on dividends received (amounting to Rs. 40) is included in cash flows from investing activities and the balance of Rs. 860 is included in cash flows from operating activities.

(5) *Repayment of Long-term Borrowings*

Long-term Debts at the beginning of the year	1,040
Add : Long-term Borrowings made during the year	250
	1,290
Less : Long-term Borrowings at the end of the year	1,110
	180

(6) *Interest paid*

Interest expense for the year	400
Add: Interest Payable at the beginning of the year	100
	500
Less: Interest Payable at the end of the year	230
	270

Terms Introduced in the Chapter

1. Cash
2. Cash Equivalent
3. Cash Inflows
4. Cash Outflows
5. Non-cash item
6. Cash Flow Statement
7. Operating Activities
8. Investing Activities
9. Financing Activities
10. Accounting Standard 3
11. Extraordinary Items

Summary

Cash Flow Statement: The Cash Flow Statement is considered to be superior to Statement of Changes in Financial Position to ascertain the liquidity of an enterprise. Cash Flow Statement is to be prepared and reported by Indian enterprises according to AS-3 issued by The Institute of Chartered Accountants of India. The cash flows are categorised into flows from operating, investing and financing activities. This statement helps the users to ascertain the amount and certainty of cash flows to be generated by an enterprise.

Question for Practice

A. Short Answer Questions

1. What is a Cash flow statement?
2. How the varions activities are classified (as per AS-3 revised) while preparing cash flow statement?
3. State the uses of cash flow statement?
4. What are the objectives of preparing cash flow statement.
5. Explain the terms: Cash Equivalents, Cash flows.
6. Prepare a format of cash flow from operating activities under direct method and indirect method.
7. Now that you know the meaning of operating activities, state clearly what would constitute the operating activities for the following types of enterprises:
   - (i) Hotel
   - (ii) Film production house
   - (iii) Financial enterprise
   - (iv) Media enterprise
   - (v) Steel manufacturing unit
   - (vi) Software business unit.
8. "The nature/type of enterprise can change altogether the category into which a particular activity may be classified." Do you agree? Illustrate your answer.

B. Long Answer Questions

1. Describe the procedure to prepare Cash Flow Statement.
2. Describe "Direct" and "Indirect" method of ascertaining Cash Flow from operating activities.
3. Explain the major Cash Inflow and outflows from investing activities.
4. Explain the major Cash Inflows and outflows from financing activities.

Numerical Questions

1. Anand Ltd. arrived at a net income of Rs. 5,00,000 for the year ended March 31, 2007. Depreciation for the year was Rs. 2,00,000. There was again of Rs. 50,000 on assets sold which was credited to profit and loss account. Bills Receivables increased during the year Rs. 40,000 and Bills Payables also increased by Rs. 60,000. Compute the cash flow operating activities by the indirect approach.
2. From the information given below you are required to prepare the cash paid for the inventory:

	(Rs.)
Inventory in the beginning	40,000
Purchases	1,60,000
Inventory in the end	38,000
Inventory creditors in the beginning	14,000
Inventory creditors in the end	14,500

[**Ans.:** Rs. 1,59,500]

3. For each of the following transactions, calculate the resulting cash flow and state the nature of cash flow viz., operating, investing and financing.

(a) Acquired machinery for Rs. 2,50,000 paying 20% drawn and executing a bond for the balance payable.

(b) Paid Rs. 2,50,000 to acquire shares in Informa Tech. and received a dividend of Rs. 50,000 after acquisition.

(c) Sold machinery of original cost Rs. 2,00,000 with an accumulated depreciation of Rs. 1,60,000 for Rs. 60,000.

[**Ans.:** Rs. 50,000 investing flow (outflow); Rs. 2,00,000 investing flow (outflow); Rs. 60,000 investing flow (inflow).].

4. The following is the Profit and Loss Account of Yamuna Limited:

Yamuna Limited
Profit and Loss Account for the Year ended March 31, 2007

	(Rs.)	(Rs.)
Sales		10,00,000
Cost of Goods Sold:		
Opening Stock	2,50,000	
Purchases	5,00,000	
	7,50,000	
Less Closing Stock	2,00,000	5,50,000
Gross Profit		4,50,000
Operating Expenses		3,00,000
Net Profit		1,50,000

Additional information:

(i) Trade debtors decrease by Rs. 30,000 during the year.
(ii) Prepaid expenses increase by Rs. 5,000 during the year.
(iii) Trade creditors decrease by Rs. 15,000 during the year.
(iv) Outstanding expenses increased by Rs. 3,000 during the year.
(v) Operating expenses included depreciation of Rs. 25,000.

Compute net cash provided by operations for the year ended March 31, 2007 by the indirect method.

[**Ans.:** Cash provided from operations Rs. 2,18,000].

5. Compute cash from operations from the following figures:

(i) Profit for the year 2005-06 is a sum of Rs. 10,000 after providing for depreciation of Rs. 2,000.

(ii) The current assets of the business for the year ended March 31, 2006 and 2007 are as follows:

	March 31, 2006 (Rs.)	*March 31, 2007* (Rs.)
Debtors	10,000	12,000
Provision for Doubtful Debts	1,000	1,200
Bills Receivables	4,000	3,000
Bills Payables	5,000	6,000
Creditors	8,000	9,000
Inventories	5,000	8,000
Short-term Investments	10,000	12,000
Outstanding Expenses	1,000	1,500
Prepaid Expenses	2,000	1,000
Accrued Income	3,000	4,000
Income received in advance	2,000	1,000

[**Ans.:** Cash from operations: Rs. 7,700].

Preparation of Cash Flow Statement from Summary Cash Account

6. From the following particulars of Bharat Gas Limited, calculate Cash Flows from Investing Activities. Also show the workings clearly preparing the ledger accounts:

Balance Sheet of Bharat Gas Limited as on ....

Liabilities	2006 Amount (Rs.)	2007 Amount (Rs.)		2006 Amount (Rs.)	2007 Amount (Rs.)
			Goodwill	1,00,000	3,00,000
			Patents	2,80,000	1,60,000
			Machinery	10,20,000	12,40,000
			10% Long-term investment	60,000	1,60,000
			Investment in land	1,00,000	1,00,000
			Shares of Amartax Ltd.	1,00,000	1,00,000

Additional Information:

(a) Patents were written off to the extent of Rs. 40,000 and some Patents were sold at a profit of Rs. 20,000.

(b) A Machine costing Rs. 1,40,000 (Depreciation provided thereon Rs. 60,000) was sold for Rs. 50,000. Depreciation charged during the year was Rs. 1,40,000.

(c) On March 31, 2007, 10% Investments were purchased for Rs. 1,80,000 and some Investments were sold at a profit of Rs. 20,000. Interest on Investment was received on March 31, 2007.

(d) Amartax Ltd. paid Dividend @ 10% on its shares.

(e) A plot of Land had been purchased for investment purposes and let out for commercial use and rent received Rs. 30,000.

[**Ans.:** Rs. 5,24,200].

7. From the following Balance Sheet of Mohan Ltd. Prepare cash flow Statement:

Balance Sheet of Rajeshwar Limited as on ....

Liabilities	2005 (Rs.)	2006 (Rs.)	*Assets*	2005 (Rs.)	2006 (Rs.)
Equity Share Capital	2,00,000	3,00,000	Fixed Assets	4,00,000	6,00,000
Profit & Loss	1,60,000	2,00,000	Stock	1,30,000	1,50,000
Bank Loan	1,00,000	80,000	Debtor's	1,00,000	60,000
Accumulated Dep.	80,000	1,00,000	Bills Receivable	20,000	30,000
Creditor	1,40,000	1,20,000	Bank	90,000	30,000
Proposed Dividend	60,000	70,000			
	7,40,000	**8,70,000**		**7,40,000**	**8,70,000**

Additional Information:

Machine Costing Rs. 80,000 on which accumulated depreciation was Rs, 50,000 was sold for Rs. 20,000.

[**Ans.:** Cash flow from Operating Activity Rs. 1,80,000
Cash flow from Invisiting Activity Rs. (2,60,000)
Cash flow from Financing Activity Rs. 20,000].

8. From the following Balance Sheets of Tiger Super Steel Ltd., prepare Cash Flow Statement:

Balance Sheet

Liabilities	2005 (Rs.)	2006 (Rs.)	*Assets*	2005 (Rs.)	2006 (Rs.)
Equity Share Capital	80,000	1,20,000	Goodwill	24,000	18,800
10%Preference Sh. Capital	40,000	20,000	Land & Building	40,000	20,000
General Reserve	8,000	12,000	Plant	36,000	76,400
Profit and Loss Account	7,200	10,800	Investment	4,000	14,000
Proposed Dividend	11,200	15,600	Debtor's	30,000	43,200
Bills Payable	14,000	21,200	Stock	34,000	31,200
Outstanding Expenses	3,200	2,400	Cash	6,800	11,200
Provision for Taxation	11,200	12,800			
	1,74,800	**2,14,800**		**1,74,800**	**2,14,800**

Additional Information:

Depreciation Charge on Land & Building Rs. 20,000, and Plant Rs. 10,000 during the year.

[**Ans.:** Cash flow from Operating Activities Rs. 34,800
Cash flow from Invisiting Activities Rs. (50,400)
Cash flow from Financing Activities Rs. 20,000].

9. Prepare Cash Flow Statement from the following Information:

Balance Sheet

Liabilities	2004 (Rs.)	2005 (Rs.)	*Assets*	2004 (Rs.)	2005 (Rs.)
Equity Share Capital	5,00,000	7,00,000	Cash/Bank	3,00,000	4,00,000
8% Debentures	6,00,000	4,00,000	Sundry Debtor	4,00,000	6,00,000
Profit and Loss Account	3,00,000	5,00,000	Stock	5,00,000	6,00,000
Creditor	6,00,000	9,00,000	Goodwill	2,50,000	1,70,000
			Discount on Debenture	50,000	30,000
			Plant	5,00,000	7,00,000
	20,00,000	**25,00,000**		**20,00,000**	**25,00,000**

Additional Information:

Depreciation Charge on Plant amount to Rs. 80,000.

[**Ans.:** Cash inflow from Operating Activities Rs. 3,80,000
Cash inflow from Invisiting Activities Rs. (2,80,000)
Cash inflow from Financing Activities Rs. — NIL].

10. From the following Information Prepare Cash flow Statements for Yogeta Ltd.

Balance Sheet

Liabilities	*2005 (Rs.)*	*2006 (Rs.)*	*Assets*	*2005 (Rs.)*	*2006 (Rs.)*
Equity Share Capital	2,00,000	3,00,000	Bank	45,000	-
Preference Share Capital	–	1,00,000	Cash	5,000	-
Profit and Loss Account	1,00,000	2,00,000	Stock	1,00,000	1,70,000
Loan	2,00,000	–	Bills Receivable	50,000	1,00,000
Provision for Taxation	30,000	50,000	Fixed Assets	4,00,000	7,00,000
Bills Payable	50,000	70,000			
Bank overdraft	–	1,00,000			
Loan from Rahul	20,000	1,50,000			
	6,00,000	**9,70,000**		**6,00,000**	**9,70,000**

Additional Information:

Net Profit for the year After Charging Rs. 50,000 as Depreciation was Rs. 1,50,000. Dividend paid on Share was Rs. 50,000, Tax Provision created during the year year amounted to Rs. 60,000.

[**Ans.:** Cash from Operating Activities Rs. 2,20,000
Cash from Invisiting Activities Rs. (3,50,000)
Cash from Financing Activities Rs. (80,000)].

11. Following is the Financial Statement of Garima Ltd. Prepare Cash flow Statements.

Balance Sheet as on 31st Dec. 2006

Liabilities	*2005 (Rs.)*	*2006 (Rs.)*	*Assets*	*2005 (Rs.)*	*2006 (Rs.)*
Equity Share Capital	2,00,000	3,00,000	Plant & Machinery	2,00,000	3,64,000
Preference Share Capital	80,000	1,40,000	Stock	60,000	1,60,000
Creditor	56,000	1,56,000	Debtor	20,000	80,000
Provision for Taxation	4,000	12,000	Bank	80,000	28,000
Profit & Loss Account	28,000	40,000	Prepaid Expenses	8,000	16,000
	3,68,000	**6,48,000**		**3,68,000**	**6,48,000**

Profit and Loss Account for the Year ended Dec. 31, 2006

Receipts	*Amount (Rs.)*	*Payments*	*Amount (Rs.)*
Opening Stock	60,000	Sales	5,00,000
Purchase	4,92,000	Closing Stock	1,60,000
Gross Profit c/d	1,08,000		
	6,60,000		**6,60,000**
Salary	44,000	Gross Profit b/d	1,08,000
Depreciation	32,000		
Provision for Tax	16,000		
Net profit c/d	16,000		
	1,08,000		**1,08,000**
Dividend	4,000	Balance b/d	28,000
Balance c/d	40,000	Net Profit b/d	16,000
	44,000		**44,000**

[**Ans.:** Cash Outflow (use) from Operating Activities Rs. (12,000)
Cash flow from Investing Activities Rs. (1,96,000)
Cash flow from Financing Activities Rs. (1,56,000)].

12. Following as the Balance Sheets of Computer India Ltd.:

(In Lakhs)

Liabilities	*2004 (Rs.)*	*2005 (Rs.)*	*Assets*	*2004 (Rs.)*	*2005 (Rs.)*
Equity Share Capital	40,000	50,000	Fixed Assets	41,000	40,000
Profit and Loss Account	1,000	1,200	*Less :* Provision for Depreciation	11,000	15,000
General Reserve	2,000	2,500		**30,000**	**25,000**
10% Debentures	6,000	6,500	Debtors	20,000	24,000
Sundry Creditor	12,000	11,000	Stock	30,000	35,000
Provision for Taxation	3,000	4,200	Prepaid Expenses	300	500
Proposed Dividend	5,000	5,800	Cash	1,200	3,500
Bank overdraft	12,500	6,800			
	81,500	**88,000**		**81,500**	**88,000**

Additional Information:

Interest paid on Debenture Rs. 600

[**Ans.:** Net Cash from Operating Activities Rs. 2,100
Net Cash from Invisiting Activities Rs. 1,000
Net Cash from Financing Activities Rs. 4,900].

Project Work

1. Read and analyse the cash flow statements as given in the Annual Report of any three listed companies (say Arvind Mills, Infosys, Tisco, etc.) and ascertain:
   - (i) which method (direct or indirect) is used for the purpose of calculating cash flows from operating activities;
   - (ii) the treatment of special items such as dividend tax, profit/loss on sale of fixed assets, depreciation of extraordinary items, etc.
   - (iii) Whether all companies follow the same proforma of cash flow statement or different ones.
   - (iv) As to whether you think that companies properly highlight cash flow statement in their Annual Reports.
2. "Every enterprise must necessarily prepare and present a statement of cash flows". Discuss it in the classroom.
3. You analyse the cash flow statement for the past 3 years for Madrid Ltd. and find that-
   - (i) there has been net increase in cash and cash equivalents over the years.
   - (ii) However, net cash flow from operating activities have been negative throughout. What may be the possible reasons for the above mentioned situation. What would be your perception about the functioning of the company.

Answers to Test your Understanding

Test your Understanding – I

Answer : a) Operating activities - 3, 6, 7, 10, 13, 15, 19, 20, 23, 24, 27;
b) Investing activities - 1, 5, 8, 11, 12, 16, 17, 21, 22, 29;
c) Financing activities - 2, 4, 9, 14, 18, 25, 26, 28;
d) Cash equivalents - 30, 31, 32, 33.

Test your Understanding – II

Answers: 1. 40,000, 2. 60,000, 3. deducted from,

4. deducted from, 5. added to, 7. added to

Answers: 1. +, 2. NC, 3. +, 4. -, 5. +, 6. NC, 7. -, 8 +, 9. NC, 10 -, 11 -, 12 +

APPENDIX - 1

GRASIM INDUSTRIES LIMITED

Cash flow statement for the year ended 31st March, 2000

Rs. in Crores

	Current Year		*Previous Year*	
A. Cash Flow from Operating Activities				
a. Net profit before tax and exception item	1201.90		1361.36	
Adjustment for :				
Depreciation	291.64		284.57	
Interest expenses	97.32		138.76	
Interest Income	(29.48)		(75.38)	
Dividend Income	(38.04)		(39.37)	
Write down in value of Assets held for disposal	–		7.00	
Profit/Loss on sale of Fixed Assets (Net)	3.99		(2.25)	
Profit on sale of Long Term Investment (Net)	(62.57)		(24.90)	
Profit on sale of Current Investments (Net)	(7.27)		(3.37)	
b. Operating profit before working capital changes	1457.49		1646.42	
Adjustments for:				
Trade and other receivables	116.66		(78.33)	
Inventories	(72.14)		(219.13)	
Assets Held for Disposal	0.97		1.84	
Trade Payables	159.70		90.96	
c. Cash generated from Operations	1662.68		1441.76	
Direct Taxes Paid (Net)	(380.42)		(391.30)	
Cash from operating activities before exceptional item	1282.26		1050.46	
Net Cash from Operating Activities		1282.26		1050.46
B. Cash Flow from Investing Activities				
Purchase of fixed assets	(408.80)		(301.75)	
Sale of fixed assets	9.29		19.71	
Purchase of Investments	(502.03)		(75.41)	
Sale of Investments	72.19		669.49	
Investments/Advances in Joint Ventures, Subsidiaries & Others	(119.31)		(1294.14)	
Interest received	29.11		74.29	
Dividend received	38.04		39.37	
Net Cash from/(used in) investing activities		(881.51)		(868.44)
C. Cash Flow from Financing Activities				
Proceeds from borrowings	128.25		326.40	
Repayments of borrowings	(181.58)		(354.13)	
Interest paid	(112.71)		(150.11)	
Dividends paid	(145.25)		(128.19)	
Corporate dividend tax	(20.58)		(16.77)	
Net Cash from/(used in) financing activities		(331.87)		(322.80)
D. Net increase/(Decrease) in Cash and Cash equivalent		68.88		(140.78)
Cash and Cash equivalent at the beginning of the year		86.70		227.48
Cash and Cash equivalent at the end of the year		155.58		86.70
(Cash and cash equivalent represent Cash and Bank balances)				

Note:

1. Previous years' figures have been regrouped/recast wherever necessary

APPENDIX - 2

UCAL FUEL SYSTEMS LIMITED
Cash Flow Statement for the year ended 31st March, 2000

	For the year ended 31.3.2006	*For the year ended 31.3.2005*
	Rs. in '000	
A. Cash Flow from Operating Activities		
Net Profit before tax and extraordinary items	241,438	359,488
Adjustment for :		
Miscellaneous Expenditure written-off	12,826	3,330
Depreciation/Assets Discarded	129,948	134,530
Interest Income	(2,285)	(3,185)
Dividend Income	(12,910)	(12,590)
Interest Expense	59,968	4,634
Operating Profit before Working Capital changes	428,985	486,207
Adjustments for :		
Debtors	30,912	44,225
Inventories	10,620	(53,446)
Loans and Advances	30,051	(44,039)
Trade Payables	26,337	(76,138)
Prior Period Adjustments	671	323
Cash generated from Operations	527,576	357,132
Income - Tax paid	(90,594)	(92,962)
Net cash from Operating Activities - "A"	436,982	264,170
B. Cash flow from Investing Activities		
Purchase of Fixed Assets	(85,586)	(221,417)
Product Development & Research Expenses	(71,238)	(71,133)
Capital Work-In-Progress	(46,346)	146,329
Sale of Fixed Assets	3,154	4,091
Sale of Investments	281,120	4,750
Purchase of Investments	(1,068,690)	(35,000)
Interest Received	3,355	2,837
Dividend Received	12,909	12,590
Net cash from Operating Activities - "B"	(971,322)	(156,953)
C. Cash flow from Financing Activities		
Proceeds from Borrowings/Repayment of Loans	686,633	(44,251)
Dividend paid including Tax on Dividend	(79,225)	(62,777)
Interest Paid	(61,456)	(4,294)
Net cash used in Financing Activities - "C"	545,952	(111,322)
Net increase in Cash and Cash Equivalents - "A+B+C"	11,612	(4,105)
Cash and Cash Equivalents as at the beginning	62,950	67,055
Cash and Cash Equivalents as at the end	74,562	62,950

APPENDIX - 3

STERLITE OPTICAL TECHNOLOGIES LIMITED
Cash Flow Statement for the year ended March 31, 2006

		2006 (Rs. in Million)	2005 (Rs. in Million)
A. Cash Flow from Operating Activities			
Net Profit after tax as per Profit & Loss Account	407.66		102.20
Adjustment for Taxation	(26.10)		0.32
		381.56	102.52
Adjustments for :			
- Depreciation	289.92		266.76
- Investment Written-off & Loss On Sale of Investment	-		0.41
- Interest Expenses (net)	161.36		104.12
- (Profit)/Loss on Sale of Assets	(1.49)		2.52
- Gain on prepayment of Deferred Sales Tax Liability	(146.60)		-
- Provisions and Write-off	-		16,80
		303.19	
Operating profit before working capital changes		684.75	493.13
Adjustments for :			
- (Increase)/Decrease in Trade and Other receivables	(661.23)		(777.17)
- (Increase)/Decrease in Inventories	(85.14)		(83.02)
- Increase/(Decrease) in Trade Payables	(161.14)	(907.51)	941.55
Cash generated from operations		(222.76)	574.49
Direct taxes (paid/TDS deducted)/Refund received		(35.25)	13.68
Net Cash flow from Operating Activities		(258.01)	588.17
B. Cash flow from Investing Activities			
Purchases of Fixed Assets (Including Capital Work in Progress)		(48.95)	(67.81)
Proceeds from Sale of Fixed Assets		3.21	14.48
(Purchase)/Sale of Investments		(0.05)	-
Investments in Bank Fixed Deposits		(491.64)	-
Application Money Paid Pending Allotment		(24.95)	-
Interest received from Subsidiary Companies		15.99	19.65
Loan to Subsidiary Companies		(100.83)	(95.58)
Net cash flow from Investing Activities		(647.22)	(129.26)
C. Cash flow from Financing Activities			
Proceeds/(Repayment) of Secured Loans (net)		1,175.73	(89.92)
Proceeds/(Repayment) of Preferential Equity Issue & Share Warrants		336.00	-
Proceeds/(Repayment) of Unsecured Loans (net)		(117.62)	(120.71)
Interest paid		(163.43)	(123.77)
Payment of Unclaimed Dividend		(0.03)	(0.09)
Net Cash flow from Financing Activities		1,230.65	(334.49)
Net Increase in cash and cash equivalent		325.42	124.42
Cash and cash equivalent as at beginning of the year		137.66	13.24
Cash and cash equivalent as at the year end		463.08	137.66

Notes