UNIT III

SUBJECT NAME	SUBJECT CODE	SEMESTER	PREPARED BY
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FUNDS ANALYSIS

Funds Flow Statement

The basic financial statements, i.e., the balance sheet and profit and loss account or income statement of business, reveal the net effect of the various transactions on the operational and financial position of the company. It reveals the financial status of the company. The profit and loss account reflects the results of the business operations for a period of time. It contains a summary of expenses incurred and the revenues realised in an accounting period. Both these statements provide the essential basic information on the financial activities of a business, but their usefulness is limited for analysis and planning purposes. The balance sheet does not disclose the causes for changes in the assets and liabilities between two different points of time, The profit and loss account in a general way, indicates the resources provided by operations. But there are many transactions that take place in an undertaking and which do not operate through profit and Loss account. Thus, another statement has to be prepared to show the change in the assets and liabilities from the end of one period of time to the end of another period of time. The statement is called a Statement of changes in Financial Position or a Funds Flow Statement.

The Funds Flow Statement is a statement which shows the movement of funds and is a report of the financial operations of the business undertaking. It indicates various means by which funds were obtained during a particular period and the ways to which these funds were employed. In simple words, it is a statement of sources and applications of funds.

MEANING AND CONCEPT OF FUNDS

The term ‘funds’ has been defined in a number of ways.

(a) In a narrow sense, it means cash only and a funds flow statement prepared on this basis is called a cash flow statement, Such a statement enumerates net effects of the various business transactions on cash and takes into account receipts and disbursements of cash.

(b) In a broader sense, the term ‘funds’ refers to money values to whatever form it may exist. Here ‘funds’ means all financial resources, used in business whether in the form of men, material, money, machinery and others.

(c) In a popular sense the term ‘funds’ means working capital, i.e., the excess of current assets over current liabilities. The working capital concept of funds has emerged due to the fact that total resources of a business are invested partly in fixed assets in the form of fixed capital and partly kept in form of liquid or near liquid form as working capital.

Meaning and Concept of ‘Flow of Funds’

The term ‘flow’ means movement and includes both ‘inflow’ and ‘outflow’. The term ‘flow of funds’ means transfer of economic values from one asset of equity to another . Flow of funds is said to have taken place when any transaction makes changes in the amount of funds available before happening of the transaction. If the effect of transaction results in the increase of funds, it is called as source of funds and if it results in the decrease of funds, it is known as an application of funds. Further, in case the transaction does not change funds, it is said to have not resulted in the flow of funds.

Rule

The flow of funds occurs when a transaction changes on the one hand a non- current account and on the other a current account and vice-versa, When a change in a non-current account e.g., fixed assets, long-term liabilities, reserves and surplus, fictitious assets, etc., is followed by a change in another non-current account, it does not amount to flow of funds, This is because of the fact that ‘in such cases neither the working capital increases nor decreases. Similarly when a change in one current account results in a change in another current account, it does not affect funds. Funds move from noncurrent to current transactions or vice-versa only. In simple language funds move when a transaction affects (i) a current asset and a fixed asset, or (ii) a fixed and a current liability, or (iii) a current asset and (iv) fixed liability, or (v) a fixed liability and current liability; and funds do not move when the transaction affects fixed assets and fixed liability or current assets and current liabilities.

To understand flow of funds, it is essential to classify various accounts and balance sheet items into current and non-current categories,

Current Accounts can either be current assets or current liabilities, Current assets are those assets which in the ordinary course of business can be or will be converted into cash within a short period of normally one accounting year. Current Assets include - Cash in hand, Cash at bank, Bills Receivable, Sundry Debtors or Accounts Receivable, Short-term loans & advances Temporary or marketable Investments, Inventories or stocks such as (a) Raw materials (b) Work-in-process Stores and Spares (d) Finished Goods, Prepaid Expenses, Accrued Incomes etc.

Current liabilities are those liabilities which are intended to be paid in the ordinary course of business within a short period of normally one accounting year out of the current assets or the income of the business. Current Liabilities include - Bills Payable, Sundry Creditors or Accounts Payable, Accrued or Outstanding Expenses, Dividends Payable, Bank Overdraft
Short-term loans & deposits, Provision against Current Assets , Provision for taxation, if it does not amount to appropriation of profits, Proposed Dividend (May be a current or a noncurrent liability) etc.

Meaning and Definition of Funds Flow Statement

Funds Flow Statement is a method by which we study changes in the financial position of a business enterprise between beginning and ending financial statement dates. It is a statement showing sources and uses of funds for a period of time.

Foulke defines this statement as:

"A statement of sources and application of funds is a technical device designed to analyse the changes in the financial condition of a business enterprise between two dates."

In the words of Anthony, ''The funds flow statement describes the sources from which additional funds were derived and the use to which these sources were put''
Thus, funds flow statement is a statement which indicates various means by which the funds have been obtained during a certain period and the ways to which these funds have been used during that period. The term 'funds' used here means working capital, i.e. the excess of current assets over current liabilities.

Uses, Significance and Importance of Funds Flow Statement

A funds flow statement is an essential tool for the financial analysis and is of primary importance to the financial management, Now-a-days, it is being widely used by the financial analysts, credit granting institutions and financial managers. The basic purpose of a funds flow statement is to reveal the changes in the working capital on the two balance sheet dates. It also decribes the sources from which additional working capital has been financed and the uses to which working capital has been applied. Such a statement is particularly useful in assessing the growth of the firm, its resulting financial needs and in determining the best way of financing these needs. The significance or importance of a funds flow statement can be well followed from its various uses given below :

1. **It helps in the analysis of financial operations.** The balance sheet gives a static view of the resources of a business and the uses to which these resources have been put at a certain point of time. But it does not disclose the causes for changes in the assets and liabilities between two different points of time. The funds flow statement explains

causes for such changes and so the effect of these changes on the liquidity position of the company. The funds flow statement gives a clear answer to such a situation explaining what has happened to the profits of the firm.

2. **It throws light on many perplexing questions of general interest** which otherwise may be difficult to be answered, such as:
   (a) Why were the net current assets lesser in spite of higher profits and vice-versa?
   (b) Why more dividends could not be declared in spite of available profits?
   (c) How was it possible to distribute more dividends than the present earnings?
   (d) What happened to the net profit? Where did they go?
   (e) What happened to the proceeds of sale of fixed assets or issue of shares, debentures, etc.?
   (f) What are the sources of the repayment of debt?
   (g) How was the increase in working capital financed and how will it be financed in future?
3. **It helps in the formation of a realistic dividend policy.** Sometimes a firm has sufficient profits available for distribution as dividend but yet it may not be advisable to distribute dividend for lack of liquid or cash resources. In such causes, a funds flow statement helps in the formation of a realistic dividend policy.
4. **It helps in the proper allocation of resources.** The resources of a concern are always limited and it wants to make the best use of these resources. A projected funds flow statement constructed for the future help in making managerial decisions. The firm can plan the deployment of its resources and allocate them among various applications.

5. It acts as a future guide. A projected funds flow statement also acts as a guide for future to the management. The management can come to know the various problems it is going to face in near future for want of funds. The firm's future needs of funds can be projected well in advance and also the timing of these needs. The firm can arrange to finance these needs more effectively and avoid future problems.

6. It helps in appraising the use of working capital. A funds flow statement helps in explaining how efficiently the management has used its working capital and also suggests ways to improve working capital position of the firm.

7. It helps knowing the overall creditworthiness of a firm. The financial institutions and banks such as State Financial Institutions. Industrial Development Corporation, Industrial Finance Corporation of India, Industrial Development Bank of India, etc. all ask for funds flow statement constructed for a number of years before granting loans to know the creditworthiness and paying capacity of the firm. Hence, a firm seeking financial assistance from these institutions has no alternative but to prepare funds flow statements.

Limitations of Funds Flow Statement

The funds flow Statement has a number of uses, however, it has certain limitations also, which are listed below:

1. It should be remembered that a funds flow statement is not a substitute of an income statement or a balance sheet. It provides only some additional information as regards changes in working capital.
2. It cannot reveal continuous changes.
3. It is not an original statement but simply a re-arrangement of data given in the financial statement. . It is essentially historic in nature and projected funds flow statement cannot be prepared with much accuracy.
5. Changes in cash are more important and relevant for financial management than the working capital.

Procedure for Preparing a Funds Flow Statement

Funds flow statement is a method by which we study changes in the financial position of a business enterprise between beginning and ending financial statements dates. Hence, the funds flow statement is prepared by comparing two balance sheets and with the help of such other information derived from the accounts as may be needed. Broadly speaking, the preparation of a funds flow statement consists of two parts:

1. Statement or Schedule of Changes in Working Capital.
2. Statement of Sources and Application of Funds,

1. Statement or Schedule of Changes in Working Capital

Working Capital means the excess of current assets over current liabilities, Statement of changes in working capital is prepared to show the changes in the working capital between the two balance sheet dates. This statement is prepared with the help of current assets and current liabilities derived from the two balance sheets.

As, Working Capital = Current Assets –Current liabilities.

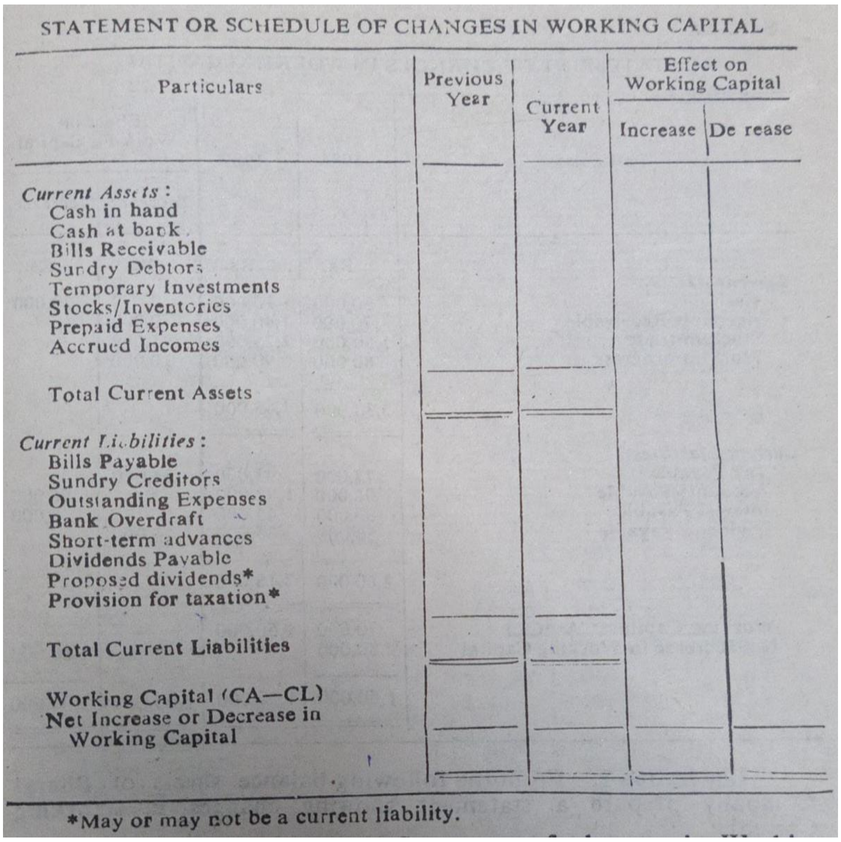
So, (i) An increase in current assets increases Working Capital;

(ii) A decrease in current assets decreases Working Capital;

(iii) An increase in Current liabilities decreases Working Capital and

(iv) A decrease in Current liabilities increases Working Capital.

STATEMENT OR SCHEDULE OF CHANGES IN WORKING CAPITAL



STATEMENT OR SCHEDULE OF CHANGES IN WORKING CAPITAL

Particulars	Previous Year	Current Year	Effect on Working Capital	
			Increase	Decrease
Current Assets :				
Cash in hand				
Cash at bank				
Bills Receivable				
Sundry Debtors				
Temporary Investments				
Stocks/Inventories				
Prepaid Expenses				
Accrued Incomes				
Total Current Assets				
Current Liabilities :				
Bills Payable				
Sundry Creditors				
Outstanding Expenses				
Bank Overdraft				
Short-term advances				
Dividends Payable				
Proposed dividends*				
Provision for taxation*				
Total Current Liabilities				
Working Capital (CA—CL)				
Net Increase or Decrease in Working Capital				

*May or may not be a current liability.

(2) Statement of Sources and Application of Funds

Funds flow statement is a statement which indicates various sources from which funds (working capital) have been obtained during a certain period and the uses or applications to which these funds have been put during that period. Generally, this statement is prepared in two formats:

(a) Report Form (b) 'T' Form or an Account Form or Self Balancing Type.

SPECIMEN OF REPORT FORM OF FUNDS FLOW STATEMENT

Sources of Funds	Rs.	**Applications or Uses of Funds**	**Rs.**
Funds from Operations		Funds Lost in Operations	
Issue of Share Capital		Redemption of Preference Share Capital	
Issue of Debentures		Redemption of Debentures	
Raising of long term loans		Repayment of long-term loans	
Receipts from partly paid shares, called up		Purchase of non-current (fixed) assets	
Sales of non-current (fixed)		Purchase of long-term	

assets		Investments	
Non-trading receipts such as dividends		Non-trading payments	
Sale of Investments (long-term)		Payments of dividends	
Net Decrease in Working Capital		Payment of tax	
		Net Increase in Working Capital	
Total		Total	

SOURCES OF FUNDS The following are the sources from which funds generally flow (come), into the business :

(1) Funds from operations or Trading Profits

Trading profits or the profits from the operations of the business are the most important and major source of funds.

Basically, there are two methods of calculating funds from operations :

1. The first method is to prepare the profit and loss account afresh by taking into consideration only fund and operational items which involve funds and are related to the normal operations of the business. The balancing figure in this case will be either funds generated from operations or funds lost in operations depending upon whether the income or credit side of profit and loss account exceeds the expense or debit side of profit and loss account or vice-versa.
2. The second method (which is generally used) is to proceed from the figure of net profit or net loss as arrived at from the profit and loss account already prepared. Funds from operations by this method can be calculated as under .

(a) Calculation of Funds From Operations

	Rs.
Closing Balance of P & L-A/c or Retained Earnings (as given in the balance sheet)	
Add: Non-fund and Non-operating items which have been already debited to P & LA/c:	
(i) Depreciation and Depletion	
(ii) Amortization of fictitious and Intangible Assets such as: (a) Goodwill (b) Patents (c) Trade Marks (d) Preliminary Expenses (e) Discount on Issue of Shares, etc.	

(iii) Appropriation of Retained Earnings such as : (a) Transfer to General Reserve (b) Dividend Equalisation Fund (c) Transfer to Sinking Fund (d) Contingency Reserve, etc.	
(iv) Loss on Sale of any non-current (fixed) assets such as : (a) Loss on sale of land and building (5) Loss on sale of machinery (c) Loss on sale of furniture (d) Loss on sale of long-term investments, etc	
(v) Dividends including: (a) Interim Dividend. (b) Proposed Dividend (if it is an appropriation of profits and not taken as current liability)	
(vi) Provision for Taxation (if it is not taken as Current Liability)	
(vii) Any other non-fund/non-operating items which have been debited to P/L a/c	
Total (A)	
Less: Non-fund or Non-operating items which have already been credited to P & L a/c	
(i)Profit or Gain from the sale of non-current (fixed) assets such as: (a)Profit on sale of land and building (b) Profit on sale of plant & machinery (c) Profit on sale of long-term investments, etc.	
(ii) Appreciation in the value of fixed assets such as increase in the value of land if it has been credited to P&L A/c	
(iii) Dividends Received	
(iv) Excess provisions retransferred to P/L A/c or written off (v) Any other non-operating item which has been credited to P/L A/c	
(vi) Opening balance of P & L A/c or Retained Earnings (as given in the balance sheet)	
Total (B)	
Total (A) - Total (B) = Funds generated by operations	

(b) Funds from operations can also be calculated by preparing Adjusted Profit and Loss Account as follows :

Adjusted Profit And Loss Account

	Rs.		**Rs.**
To Depreciation & Depletion or amortization of fictitious and intangible assets, such as: Goodwill, Patents, Trade Marks, Preliminary Expenses etc,		By Opening Balance (of P & L A/c)	

To Appropriation of Retained Earnings such as: Transfers to General Reserve, Dividend Equalisation Fund, Sinking Fund, etc.		Transfers from excess provisions	
To Loss on sale of any non-current or fixed asset		Appreciation in the value of fixed assets	
Dividends (including - interim dividend)		Dividends received	
Proposed Dividend (if not taken as a current liability)		Profit on sale of fixed of or non-current assets	
Provision for taxation (if not taken as a. current liability)		Funds from Operations (balancing figure in case debit side exceeds credit side)	
Closing balance (of P & L a/c)			
To Funds lost in Operations (balancing figure, in case credit side exceeds the debit side)			

Ex 1*:* Find out the **changes in the working capital** from the balance sheet data given below: Balance Sheet data given below :

	Dec. 31,2015	**Dec. 31,2016**
	Rs.	**Rs.**
Capital & Liabilities		
Share Capital	3,00,000	3,75,000
Trade Creditors	1,06,000	70,000
Profit and Loss A/c	14,000	31,000
	4,20,000	**4.76,000**
Assets		
Machinery	70,000	1,00,000
Stock-in-trade	1,21,000	1,36,000
Debtors	1,81,000	1,70,000
Cash	48,000	70,000
	4,20,000	**4,76,000**

Solution:

Schedule of changes in working Capital

	2015	2016	Increase in working Capital	Decrease in working Capital
Current Assets:	**Rs.**	**Rs.**	**Rs.**	**Rs.**
Cash	48,000	70,000	22,000	-
Debtors	1,81,000	1,70,000	-	11,000
Stock-in-trade	1,21,000	1,36,000	15,000	-
	3,50,000	**3,76,000**		
Current Liabilities :				
Trade Creditors	1,06,000	70,000	36,000	-
	1,06,000	**70,000**		
Working Capital (CA-CL)	2,44,000	3,06,000		
Net Increase in W.C	**62,000**			**62,000**
	3,06,000	**3,06,000**	**73,000**	**73,000**

Ex 2: Calculate Funds from operation from the following Profit and Loss account.

Profit and Loss account

	Rs.		Rs.
To Salaries	10,000	By Gross Profit	2,00,000
To Rent	3,000	By Profit on sale of Machine	5,000
To Commission	2,000	By Refund of tax	3,000
To Discount allowed	1,000	By Dividends received	2,000
To Provision for Depreciation	14,000		
To Transfers to General Reserves	20,000		
To Provision for tax	10,000		
To Loss on Sale of Investments	5000		
To Discount on Issue of Debentures	2,000		
To Preliminary Expenses	3,000		
To Selling Expenses	20,000		
To Net Profit	1,20,000		
	2,10,000		**2,10,000**

Solution: Calculation of **Funds from Operations**

		Rs.
Net Profit (as given)		**1,20,000**
Add: Non-fund or non-operating items which have been debited to Profit and Loss Account :		

	Rs.	
Provision for Depreciation	14,000	
Transfers to General Reserves	20,000	
Provision for tax	10,000	
Loss on Sale of Investments	5,000	
Discount on Issue of Debentures	2,000	
Preliminary Expenses	3,000	
		54,000
		1,74,000
Less: Non-fund or non-operating items which have been credited to P/L A/c:		
Profit on sale of machine	5,000	
Refund of tax	3,000	
Dividends Received	2,000	
		10,000
Funds from Operations		**1,64,000**

Alternatively,

Adjusted Profit and Loss Account

	Rs.		Rs.
To Provision for Depreciation	14,000	By Opening balance	-
To Transfers to General Reserves	20,000	By Profit on Sale of machine	5,000
To Provision for tax	10,000	By Refund of tax	3,000
To Loss on Sale of Investments	5,000	By Dividends Received	2,000
To Discount on Issue of Debentures	2,000	**By Funds from Operations (balancing figure)**	**1,64,000**
To Preliminary Expenses	3,000		
To Closing balance	1,20,000		
	1,74,000		**1,74,000**

Ex 3:From the following summarised balance sheets as on 31st December 2016 and 2017.

	2016	**2017**
	Rs.	Rs.
Capital :		
10% Preference share capital		
Equity share capital		
Share Premium		
Profit and Loss Account		
Liabilities (Non-Current):		
12% Debentures		
Current Liabilities :		
Creditors		
Bills Payable		
Provision for taxation		
Dividends Payable		
Total Liabilities and Capital		
Non-Current Assets		
Machinery		

Buildings		
Land		
Current Assets :		
Cash		
Debtors		
Bills Receivable		
Stock in hand		
Total Assets		

You are required to prepare a statement of sources and application of funds along with a supporting schedule of changes in Working capital. funds along with a supporting schedule of changes in working capital.

Solution:

SCHEDULE OF CHANGES IN WORKING CAPITAL

	2016	**2017**	**Increase in Working Capital**	**Decrease in Working Capital**
	Rs.	**Rs.**		
Current Assets :				
Cash	42,000	32,000	-	10,000
Debtors	38,000	38,000	-	-
Bills Receivable	42,000	62,000	20,000	-
Stock on hand	84,000	98,000	14,000	-
	2,06,000	**2,30,000**		
Current Liabilities :				
Creditors	38,000	46,000		
Bills Payable	5,000	4,000		
Provision for taxation	10,000	12,000		
Dividends Payable	7,000	8,000		
Working Capital (C.A.—C.L.)	1,46,000	1,60,000		
Net Increase in Working Capital	14,000			14,000
	1,60,000	**1,60,000**	**35,000**	**35,000**

Statement of sources and application of Funds

Sources	**Rs.**	**Applications**	**Rs.**
Issue of Preference Share Capital	10,000	Redemption of Debentures	6,000
Issue of Equity Share Capital	30,000	Purchase of Machinery (2,30,000-2,00,000)	30,000
Share Premium	6,000	Addition/Purchase of Building (1,76,000-1,50,000)	26,000
Funds from Operations	30,000	Net Increase in Working Capital	14,000
	76,000		**76,000**

Working Notes :

Calculation of Funds from Operations:

Balance of P/L A/c at the end of the year	Rs.1,34,000
Less:	
Balance of P/L A/c in the beginning of the year	Rs.1,04,000

Funds from Operations	Rs.30,000

CASH FLOW STATEMENT

The term 'funds', in a narrow sense, is used to denote cash. A Statement of changes in the financial position of firm on cash basis is called a cash flow statement. Such a statement enumerates net effects of the various business transactions on cash and takes into account receipts and disbursements of cash. A cash flow statement summarises the causes of changes in cash position of a business enterprise between dates of two balance sheets. This statement is very much similar to the statement of changes in financial position prepared on working capital basis, It is called a cash flow statement because it describes the inflow (sources) and outflow (uses) of cash.

Comparison between Funds Flow Statement and Cash Flow Statement

The term 'funds' has a variety of meanings . In a narrow sense 'it means cash and the statement of changes in the financial position prepared on cash basis is called a cash flow statement. In the most popular sense, the term 'funds' refers to working capital and a Statement of changes in the financial position prepared on this basis is called a funds flow statement. A cash flow statement is much similar to a funds flow statement as both are prepared to summarise the cases of changes in the financial position of a business. However, following are the main differences between a funds flow and a cash flow statement.

(1) Funds flow statement is based on a wider concept of funds, i.e., working capital, while cash flow statement is based on the narrower concept of funds, i.e., cash only, which is only one element of working capital, the others being debtors, stock, temporary investment, bills receivable, etc.

(2) Funds flow statement is based on accrual basis of accounting while cash flow statement is based on cash basis of accounting. In cash flow statement while calculating operating profits, adjustments for prepaid and outstanding expenses and incomes are made to convert the data

from accrual basis to cash basis ; but no such adjustments are required to be made while preparing a funds flow statement.

(3) A funds flow statement does not reveal changes in current assets and current liabilities, rather these appear separately in a schedule of changes in working capital. No such schedule of changes in working capital is prepared for a cash flow statement and changes in all assets and liabilities fixed as well as current, are summarised in the cash flow statement.

(4) Cash flow statement is prepared by taking the opening balance of cash, adding to this all the inflows of cash and deducting the outflows of cash from the total. The balance, i.e., opening balances of cash and inflows of cash—outflows of cash, is reconciled with the closing balance of cash. No such opening or closing balances appear in a funds flow statement. The net difference between sources and applications of funds does not represent cash rather it reveals the net increase or decrease in working capital.

(5) Funds flow statement is useful in planning intermediate and long-term financing while a cash flow statement is more useful for short-term analysis and cash planning of the business.

Uses and Significance of Cash Flow Statement

Cash flow statement is of vital importance to the financial management. It is an essential tool of financial analysis for short term planning. The chief advantages of cash flow statement are as follows :

(1) Since a cash flow statement is based on the cash basis of accounting, it is very useful in the evaluation of cash position of a firm.

(2) A projected cash flow statement can be prepared in order to know the future cash position of a concern so as to enable a firm to plan and coordinate its financial operations properly. By preparing this statement, a firm can come to know as to how much cash will be generated into the firm and how much cash will be needed to make various payments and hence the firm - can well plan to arrange for the future requirements of cash.

(3) A comparison of the historical and projected cash flow statements can be made so as to find the variations and the deficiency or otherwise in the performance w as to enable the firm to take immediate and effective action.

(4) A series of intra-firm and inter-firm cash flow statements reveal whether the firm's liquidity (short-term paying capacity) ie. improving or deteriorating over a period of time and 19 comparison to other firms over a given period of time.

(5) Cash flow statement helps in planning the repayment of loans, replacement of fixed assets and other similar long-term planning of cash. It is also significant for capital budgeting decisions,

(6) It better explains the causes for poor cash position in spite of substantial profits in a firm by throwing light on various applications of cash made by the firm.

(7) Cash flow analysis is more useful and appropriate than funds flow analysis for short-term financial analysis as in a very short period it is cash which is more relevant then the working capital for forecasting the ability of the firm to meet its immediate obligations.

Limitations of Cash Flow Statements

Despite a number of uses, Cash flow statements suffer from the following limitations :

(a) It is difficult to precisely define the term ‘cash’. There are controversies over a number of items like cheques, stamps, postal orders, etc. to be included in cash.

(b)A Cash flow statement reveals the inflow and outflow of cash but the exclusion of near cash items from cash conceals the true reporting of the firm’s liquidity position.

(c) Working Capital being a wider concept of funds, a funds flow statement presents a more complete picture than cash flow statement,

Procedure for Preparing a Cash Flow Statement

The preparation of cash flow statement involves the determining of:

(a) Inflows of cash. (b) Outflows of cash.

(a) Sources of Cash Inflows

The main sources of cash inflows are:

(1) Cash flow from, Operations. (2) Increase in existing liabilities of creation of new liabilities.(3) Reduction in or Sale of Assets. (4) Non-trading Receipts.

(b) Application of Cash or Cash Outflows (1) Cash lost in operations. ; (2) Decrease in or discharge of liabilities. (3) Increase in or purchase of assets, (4) Non-trading payments.

Generally, cash flow statement is prepared in two forms:

(a) Report form - (b) T Form or an Account Form or Self Balancing Type.

SPECIMEN OF REPORT FORM OF CASH FLOW STATEMENT

	Rs.		Rs.
Cash balance in the beginning		***Applications or Outflow of cash:***	
Add : Cash inflows :		Redemption of Preference shares	
Cash flow from operations		Redemption of debentures	
Sale of assets		Repayment of loans	
Issue of shares		Purchase of assets	
Issue of debentures		Payment of dividend	
Raising of loans		Payment of taxes	
Collection from debtors		Cash lost in operations	

Non trading receipts such as : Dividend received			
Income-tax refund			
		Cash Balance at the end	

How to Calculate Cash from Operations or Cash Operations Profit ?

There are three methods of determining cash from operations:

(1) From Cash Sales - Cash from operations can be calculated by deducting cash purchases and cash operating expenses from cash sales, i.e., Cash from Operations = (Cash Sales) - (Cash Purchases + Cash Operating Expenses).

CALCULATION OF CASH FROM OPERATIONS

Sales
Less : Credit Sales or Increase in accounts receivables, i e., Cash Sales
Less: Cash Purchases (Purchases - Credit Purchases or increase in payables)
Less : Cash Operating expenses (after adjusting prepaid and Outstanding expenses)
Cash from Trading Operations

2) From Net Profit/Net Loss - Cash from operations can also be calculated with the help of net profit or net loss. Under this method, net profit or net loss is adjusted for non-cash and non-operating expenses and incomes as follows:

Calculation of Cash From Trading Operations
Net Profit (as given)

Add: Non cash and non-operating items which have already been debited to P/L A/c.

Depreciation, Transfer to Reserves, Transfer to Provision, Goodwill written off, Preliminary expenses written off, Other intangible assets written off, Loss on sale or disposal of fixed assets, Increase in Accounts Payable, Increase in outstanding expenses, Decrease in prepaid expenses.

Less : Non-cash and non-operating items which have already been credited to P/L a/c.: Increase in Accounts Receivables, Decrease in Outstanding Expenses, Increase in Prepaid Expenses.

Cash from operations

(3)Cash Operating Profit - Cash operating profit is also calculated with the help of net profit or net loss. The difference in this method as compared to the above discussed method is that increase or decrease in accounts payable and accounts receivable is not adjusted while finding cash from operations and it is directly shown in the cash flow statement as an inflow or outflow of cash as the case may be. The cash from operations so calculated is generally called operating profit.

CALCULATION OF CASH OPERATING PROFIT

Net Profit (as given) or Closing Balance of Profit and Loss A/c

Add: non-cash and non-operating items which have already been to debited to P/L A/c:

Depreciation, Transfers to Reserves and Provisions, Writing off intangible assets, Outstanding Expenses (current year), Prepaid Expenses (previous year), Loss on Sale of fixed Assets, Dividend Paid, etc.

Less ; Non-cash and non-operating items which have already been credited to P/L A/c:

Profit on Sale or disposal of fixed assets, Non-trading receipts such a8 dividend received, rent received, etc., Re-transfers from provisions (excess provisions charged back), Outstanding income (current year), Pre-received incomes in previous year), Opening balance of P/L A/c.

Cash Operating Profit

Ex: 4 From the following details prepare Cash Flow statement.

	31-12-2018	**31-12-2019**		**31-12-2018**	**31-12-2019**
	Rs.	**Rs.**		**Rs.**	**Rs.**
Share Capital	70,000	74,000	Cash	9,000	7,800
Debentures	12,000	6,000	Debtors	14,900	17,700
Reserve for doubtful debts	700	800	Stock	49,200	42,700
Trade Creditors	10,360	11,840	Land	20,000	30,000
P/L A/c	10,040	10,560	Goodwill	10,000	5,000
	1,03,100	1,03,200		1,03,100	1,03,200

In addition, you are given :

(1)Dividend paid total Rs.3,500,(2) Land was purchased for Rs. 10,000. Amount provided for amortisation of goodwill Rs. 5,000, (3) Debentures paid off Rs. 6,000.

Prepare Cash Flow Statement.

Solution:

Cash Flow Statement

	Rs.		**Rs.**
Opening balance of cash on 1-1-2019	9000	Cash ***Outflows :***	
Add : Cash Inflow:		Purchase of Land	10,000
Issue of Share Capital	4000	Increase in Debtors	2,800
Increase in trade creditors	1,480	Redemption of Debentures	6,000

Cash inflow from operations	9,120	Dividends Paid	3,500
Decrease in stock	6,500	Closing balance of cash on 31-12-2019	7,800
	30,100		**30,100**

Working Notes:

Adjusted Profit and loss Account

	Rs.		Rs.
To Dividend (non- operating)	3,590	By Balance b/d	10,040
To Goodwill (non-fund/cash)	5,000	Cash inflow from operations	9,120
Reserve for doubtful debts (non-cash)	100		
Balance c/d	10,560		
	19,160		**19,160**

Ex 5. Balance Sheets of M/s A and B as on 1st January, 2018 and on 31st December 2018 were as follows:

	01/01/18	**31/12/18**		**01/01/18**	**31/12/18**
Liabilities	**Rs.**	**Rs.**	**Assets**	**Rs.**	**Rs.**
Capital	1,50,000	1,90,000	Cash	20,000	26,000
Mrs. B's Loan	30,000	-	Debtors	54,000	76,000
Loan from State Bank of India	60,000	80,000	Stock	48,000	42,000
Sundry Creditors	50,000	56,000	Furniture	2,000	2,000
			Machinery	90,000	65,000
			Land	36,000	45,000
			Building	40,000	70,000
	2,90,000	**3,26,000**		**2,90,000**	**3,26,000**

During the year a machine costing Rs. 12,000 (accumulated depreciation Rs. 4,000) was sold for Rs. 5,500. The provision for depreciation against machinery as on Ist January 2018 was Rs. 24,000 and on 3lst December, 2018 Rs. 37,000. Net profit for the year 2014 amounted to Rs. 60,000. You are required to prepare :

(a) Cash Flow Statement.
(b) Funds Flow Statement.

Solution:

(a) **Cash Flow Statement**

for the year ended 31st Dec 2018.

	Rs.		Rs.
Opening Balance of Cash on Ist January 2018	20,000	**Out flows of Cash :**	
Sources of Cash Inflow :		Repayment of Mrs B's Loan	30,000
Loan from State Bank of India	20,000	Increase in Debtors	22,000
Increase in Sundry Creditors	6,600	Purchase of Land	9,000
Decrease in Stock	6,000	Purchase of Building	30,000

Sale of machine	5,500	Drawings	20,000
Operating profit (including non-cash items)	73,500	Cash Balance on 31st Dec. 2018	26,000
	1,37,000		1,37,000

Working Notes:

Operating Profit:
(including non-fund cash item)

Net Profit for the year as given :	Rs.50,000
Add: Non-fund/cash and non-operating items:	
Depreciation on Machinery	Rs.17,000
Loss on sale of machinery	Rs.2500

	Rs.79,500

Depreciation on machinery:

Accumulated depreciation as on 1-1-2018	Rs.24,000
Less: depreciation on machinery	Rs.20,000

Sold during the year	**Rs.20,000**
Accumulated Depreciation at the end of the year on 31-12-2018	Rs.37,000

Depreciation provided during the year	**Rs.17,000**

Drawings :

Capital on 1-1-2016	Rs.1,50,000
Add: Profit for the year	Rs.60,000
	Rs.2,10,000
Less: Capital at the end of the year on 31-12-2018	Rs.1,90,000
Drawings	**Rs.20,000**

Schedule of changes in Working Capital

	1st Jan 2018	**31st Jan 2018**	**Increase in W.C**	**Decrease in W.C**
	Rs.	**Rs.**	**Rs.**	**Rs.**
Current Assets:				
Cash	20,000	26,000	6,000	-
Debtors	54,000	76,000	22,000	-
Stock	48,000	42,000	-	6,000
	1,22,000	**1,44,000**		
Current Liabilities:				
Sundry creditors	50,000	56,000		6,000
	50,000	**56,000**		
Working Capital	**72,000**	**88,000**		
Net increase in W.C	**16,000**			**16,000**
	88,000	**88,000**	**28,000**	**28,000**

Funds Flow Statement

Sources	Rs.	Applications	Rs.
Loan from S.B.I	20,000	Repayment of Mrs, B's Loan	50,000
Sale of machine	5,500	Purchase of Land	9,000
Funds from operations	**79,500**	Purchase of Buildings	30,000
		Drawings	20,000
		Net increase in W.C.	**16,000**
	1,05,000		**1,05,000**