

ACC 1701XA

Accounting for Decision Makers

LECTURE 11

Lecturer: Dr. Hanny Kusnadi

Accounting
The language of the business world



Prior Lecture 10 Refresher

- Types of Shares:
 - Ordinary Shares
 - Issuing par: ordinary shares @ par, amount above par goes into share premium account
 - Issuing no par: share capital account
 - Preferred Shares – issuing par & no par
 - Treasury Shares
 - Repurchasing is recorded at cost
 - Reissuing: if higher than cost then share premium account is used, if lower than cost then RE account is used if there is no balance in the share premium account.
 - Dividends – cash & stock dividends (small stock dividend @ fair value, large stock dividend @ par value)
- FSA:
 - EPS (Earnings per share) – mandatory disclosure on the IS
 - PE (Price Earnings) Ratio – comparison of market price to EPS
 - Dividend Payout Ratio & Dividend Yield





Chapter 14

Statement of Cash Flows

Goals for Lecture 11

Statement of Cash Flows

- Importance of Cash Flow
- Statement of Cash Flows (SCF) (LO1 & 2)
- Preparing Statement of Cash Flows
 - Cash Flow from Operations (CFO) - **Indirect Method (LO4)**
 - Cash Flow from Investing (CFI) (LO5)
 - Cash Flow from Financing (CFF) (LO5)
- Using SCF for Decision Making (LO6)

Note: Direct Method of CFO (LO7) will NOT be covered in the course, and is not examinable.

Importance of Cash



CASH IS KING!

Cash Flow is a company's ongoing ability to generate and use cash.

- **POSITIVE** Cash Flow is critical to a company's success!
 - Drives daily operations and increases purchasing power
 - Allows for expansion and new investment opportunities
 - Provides greater protection against creditors
 - Gives greater flexibility to respond to critical situations
 - Allows companies to pay dividends to owners



Importance of Cash Flow

- Without sufficient cash to fund its daily operations, even companies with high net income can go into financial trouble and end up bankrupt!



Statement of Cash Flows (SCF)

- Explains how cash (reported on the Statement of Financial Position) changes from the beginning of the period to the end of the period.
 - Where did the cash come from? Where did the cash go?
 - What explains the change in cash balance?
- Useful to help evaluate a company's ability to generate positive cash flows
- CASH includes:
 - Currency
 - Cash equivalents – short-term highly liquid investments that are readily converted into cash, usually with extremely short maturity dates (less than 3 months) such that there's little to no risk of value changing due to interest rates changes.

“Number one, Cash is King.... Number two, communicate... Number three, buy or bury the competition” Jack Welch (GE Former CEO)



Real FS

Berkshire Hathaway Cash is No Joke!

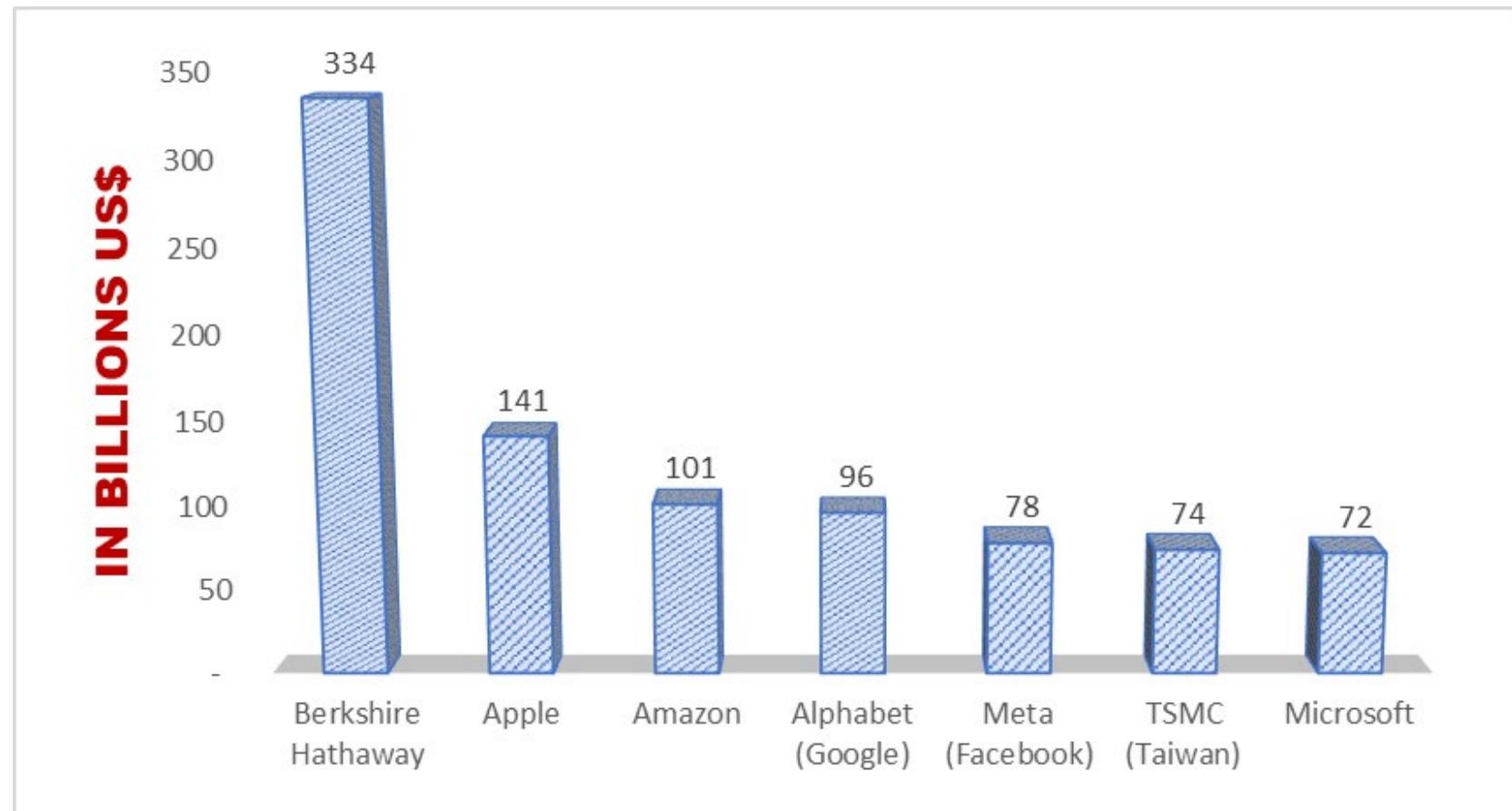
(dollars in millions)	December 31,	
	2024	2023
Assets:		
<i>Insurance and Other:</i>		
Cash and cash equivalents*	\$ 44,333	\$ 34,268
Short-term investments in U.S. Treasury Bills	286,472	129,619
Investments in fixed maturity securities	15,364	23,758
Investments in equity securities	271,588	353,842
Equity method investments	31,134	29,066
Loans and finance receivables	27,798	24,681
Other receivables	43,887	46,261
Inventories	24,008	25,856
Property, plant and equipment	30,071	30,199
Equipment held for lease	17,828	16,947
Goodwill	56,860	57,473
Other intangible assets	34,638	35,884
Deferred charges - retroactive reinsurance	8,797	9,495
Other	24,994	21,866
	917,772	839,215
<i>Railroad, Utilities and Energy:</i>		
Cash and cash equivalents*	3,396	3,754
Receivables	4,503	4,999
Property, plant and equipment	175,030	169,447
Goodwill	27,020	27,153
Regulatory assets	5,349	5,565
Other	20,811	19,845
	236,109	230,763
Total assets	<u>\$ 1,153,881</u>	<u>\$ 1,069,978</u>



SO MUCH CASH!

Companies with **huge** stockpile of cash

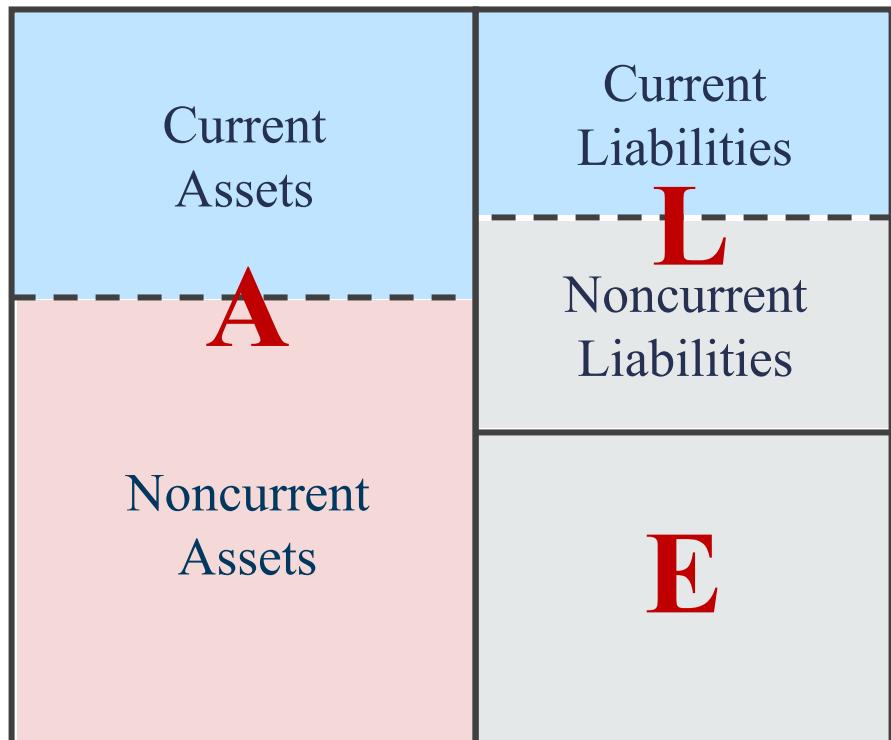
Cash and cash equivalents of the world's top cash-rich companies as at the end of FY2024



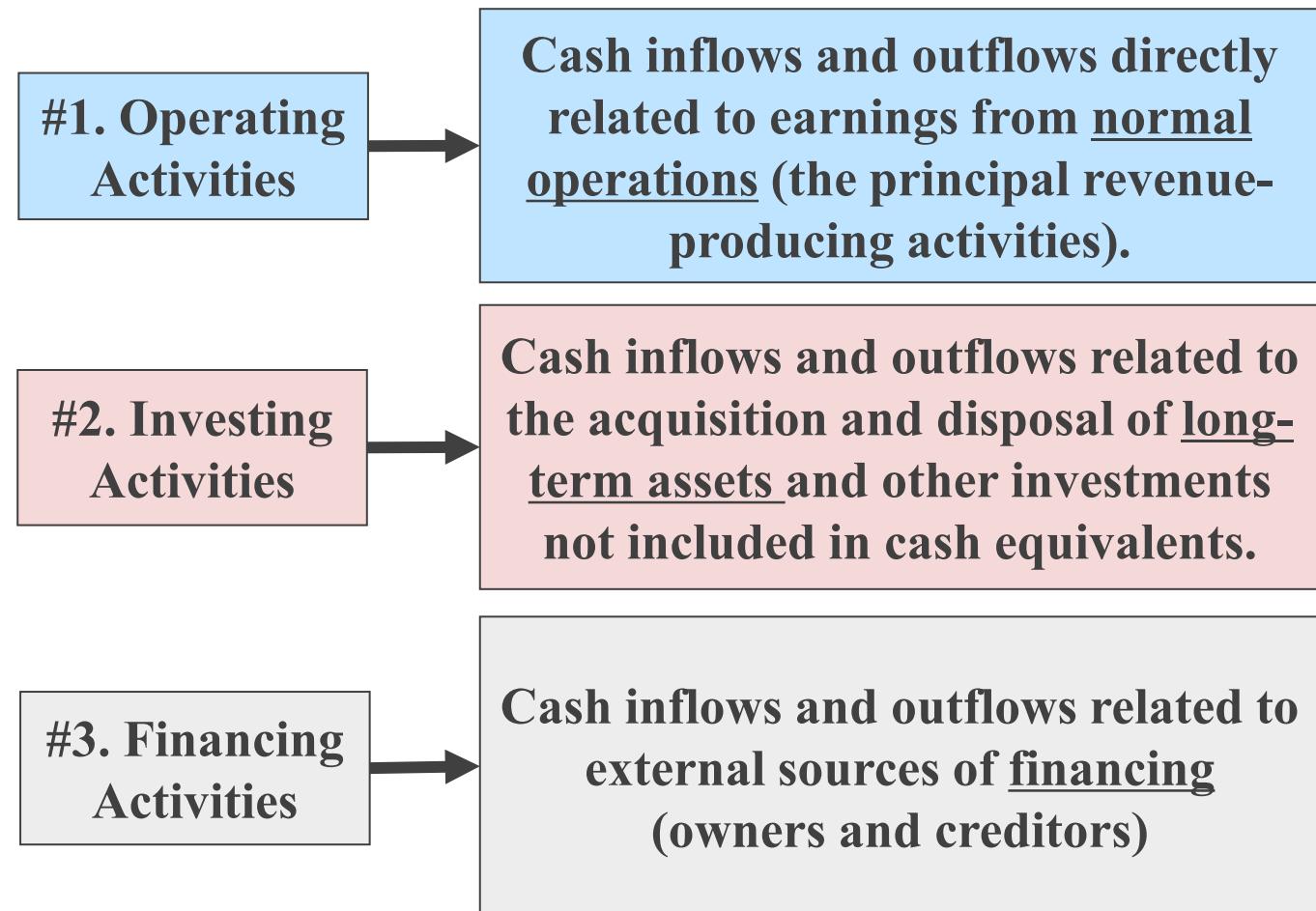
The 3 Major Activities on the SFP & Statement of Cash Flows Classification

Statement of Financial Position

$$\text{ASSETS} = \text{LIABILITIES} + \text{EQUITY}$$



Statement of Cash Flows (SCF)



#1. Cash Flows from Operating Activities (CFO)

- Cash inflows and cash outflows directly related to earnings from normal business operations (i.e. main business operations). Transactions and events that typically determine Net Income.

Inflows

Cash received from:

- Customers (from sale of goods or services)
- Royalties, fees, commission, other revenue

Outflows

Cash paid for:

- Purchase of goods and services from suppliers
- Salaries and wages
- Income taxes
- Other operating expenses (e.g. rent, utilities)



**Cash
Flows
from
Operating
Activities**

#2. Cash Flows from Investing Activities (CFI)

- Cash inflows and cash outflows related to acquisitions & disposals of long-term assets and investments.

Inflows

Cash received from:

- Sale/disposal of PPE & other LT assets
- Sale or maturity of investments in securities
- Repayment of loans made to other parties



Outflows

Cash paid for:

- Purchase of PPE and other long-term assets.
- Purchase of investments in securities
- Loans made to other parties



Cash Flows from Investing Activities

#3. Cash Flows from Financing Activities (CFF)

- Cash inflows and cash outflows related to external sources of financing (creditors & stockholders)

Inflows

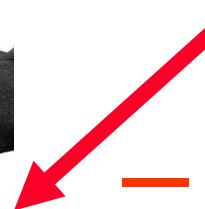
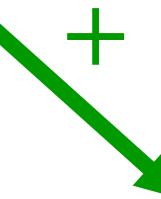
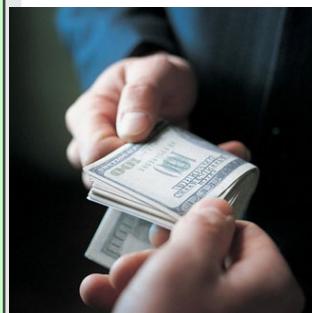
Cash received from:

- Borrowings on loans, notes, bonds, etc.
- Issuing shares to owners

Outflows

Cash paid for:

- Repayment of principal to creditors
- Repurchasing shares from shareholders
- Dividends to owners



**Cash
Flows
from
Financing
Activities**

Statement of Cash Flows

Classification of Interest & Dividends

- IFRS allow reporting entities a choice in where they want to classify interest & dividends in their SCF (as long as it is consistent):

	Operating	Investing	Financing
Interest received	Yes	Yes	
Dividends received	Yes	Yes	
Interest paid	Yes		Yes
Dividends paid	Yes		Yes

Unless otherwise stated, in this course we will assume that all interest and dividends are treated as operating cash flows, except for dividends paid which is part of financing cash flow!

NON-Cash Investing & Financing

- Investing & financing transactions that do NOT involve CASH will not appear in the SCF.
 - E.g. – acquisition of long term asset by issuing equity shares
- Such transactions need to be disclosed in the notes of the FS!

Items requiring separate disclosure include:

- **Retirement of debt by issuing equity securities.**
- **Conversion of preference shares to ordinary shares.**



Sample Format of SCF

COMPANY NAME Statement of Cash Flows For period Ended date		
Cash flows from operating activities		
[List of individual inflows and outflows]		
Net cash provided (used) by operating activities	\$ #	
Cash flows from investing activities		
[List of individual inflows and outflows]		
Net cash provided (used) by investing activities	#	
Cash flows from financing activities		
[List of individual inflows and outflows]		
Net cash provided (used) by financing activities	#	
Net increase (decrease) in cash	\$ #	
Cash (and equivalents) balance at prior period-end	#	
Cash (and equivalents) balance at current period-end	\$ #	
Separate schedule or note disclosure of any “noncash investing and financing transactions” is required.		

SCF Relationships to the SFP and IS

- We have learnt how to prepare Statement of Financial Position and Income Statement in previous chapters
- BUT, Statement of Cash Flows cannot be prepared using journal entries and accounts ledgers, because those are based on accrual accounting!
- Therefore, we must analyze the numbers from SFP and IS (under accrual basis) and adjust them to cash basis!



Information needed to prepare SCF:

- **Comparative Statements of Financial Positions.**
(current and prior year)
- **Current Income Statement.**
- **Additional details concerning selected accounts.**

#1. Cash Flows from Operations(CFO)

Indirect Vs. Direct Method

- There are **TWO** acceptable formats for presenting the CFO:

(1) Indirect Method

- Profit/loss adjusted for effects of non-cash transactions, any deferrals or accruals of past or future operating cash receipts or payments, and items of income/expense associated with investing or financing cash flows.
- Starts with accrual profit before tax and converts to cash basis
- The method **most commonly used!**

Indirect Format:

<i>Net Income</i>
<i>+/- Adjustments</i>
<i>= Operating cash flows</i>

Our Focus!

(2) Direct Method

- Reports components of cash flows from operating activities as gross receipts and gross payments.
- Preferred method for financial reporting but *RARELY USED!*

Direct Format:

<i>Cash Sales</i>
<i>- Cash Expenses</i>
<i>= Operating cash flows</i>

NOTE that no matter which format is used, the same amount of net cash flows from operating activities is generated.

#1. CFO – Indirect Method

Logic Behind the SCF Algebraic Formulation

- Recall the basic accounting equation:
$$\text{Assets} = \text{Liabilities} + \text{Shareholders' Equity}$$

- Assets are either cash (C) or not (NCA), so the equation becomes:

$$\text{Cash} + \text{Non-cash assets} = \text{Liabilities} + \text{SE}$$

- **If we look at the change in balances, the equation can be written as:**

$$\Delta \text{Cash} + \Delta \text{Non-cash assets} = \Delta \text{Liabilities} + \Delta \text{SE}$$

- After re-arranging the equation, we can express it as:

$$\Delta \text{Cash} = (\Delta \text{Liabilities} + \Delta \text{SE}) - \Delta \text{Non-cash assets}$$

- The change in cash (ΔCash) is the increase or decrease in the cash account. This amount equals changes in liabilities *plus* changes in stockholders' equity *minus* changes in assets other than cash.
- THUS, we can identify the causes in the change in the cash account by studying the changes in the non-cash accounts!



#1. CFO – Indirect Method

Logic Behind the SCF Algebraic Formulation (continued)

$$\Delta \text{Cash} = (\Delta \text{Liabilities} + \Delta \text{SE}) - \Delta \text{Non-cash assets}$$

- Expanding the equation further into current & non-current, we can get:

$$\begin{aligned}\Delta \text{Cash} = & (\Delta \text{Current Liabilities} + \Delta \text{Long-term Liabilities} + \Delta \text{SE}) \\ & - (\Delta \text{Non-cash Current assets} + \Delta \text{Long-term Assets})\end{aligned}$$

- Further expansion gives us:

$$\begin{aligned}\Delta \text{Cash} = & (\Delta \text{Current Liabilities} + \text{Issue new long-term debt} - \text{pay old long-term debt} \\ & + \text{Net income} - \text{dividend} + \text{Sales of new shares} - \text{Repurchase of shares}) \\ & - (\Delta \text{Non-cash current assets} + \text{Purchase of PPE/investment} - \text{depreciation} \\ & - (\text{Sale of PPE/investment} - \text{Gain} + \text{Loss}))\end{aligned}$$

- Re-arranging the equation will eventually give us:

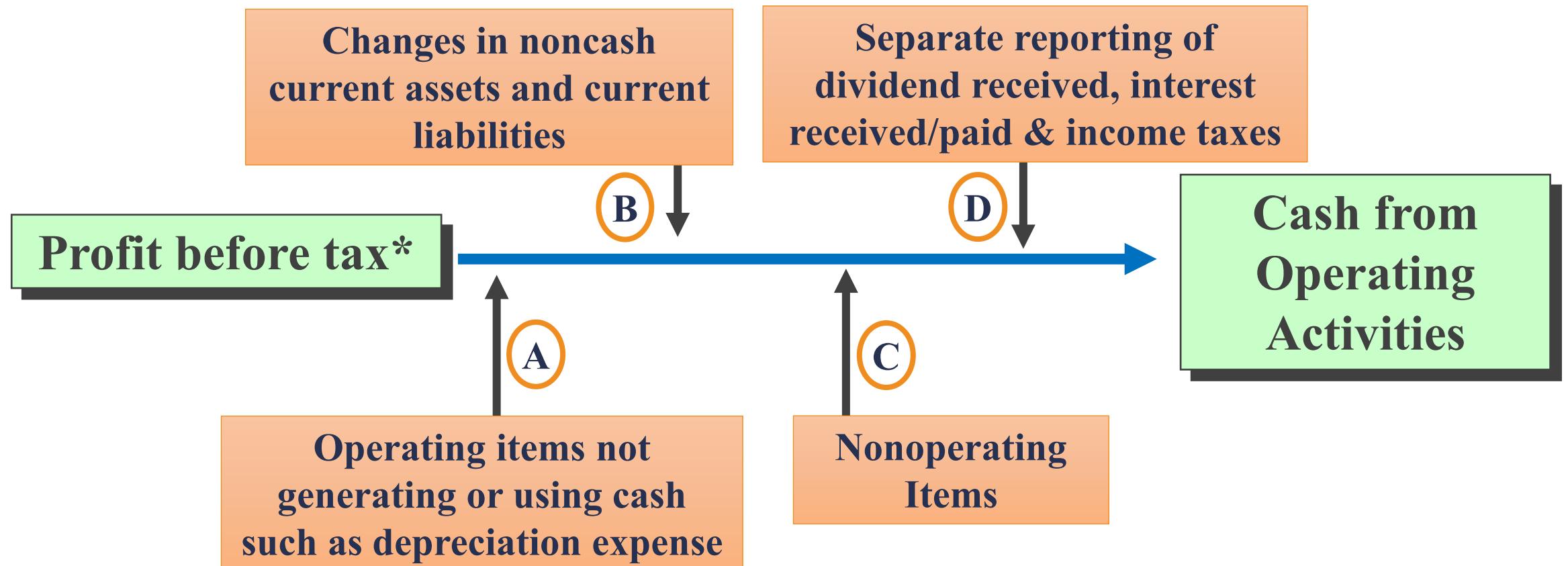

$$\begin{aligned}\Delta \text{Cash} = & \text{Net income*} + \text{Depreciation} - \text{Gain} + \text{Loss} - \Delta \text{Non-cash current assets} \\ & + \Delta \text{Current Liabilities} \\ & - \text{Purchase of PPE/investment} + \text{Sale of PPE/investment} \\ & + \text{Issue new long-term debt} - \text{Pay old long-term debt} \\ & + \text{Sales of new shares} - \text{Repurchase of shares} - \text{Dividend}\end{aligned}$$

} Operating
} Investing
} Financing

#1. CFO

The Indirect Method

- The indirect method starts with *Profit Before Tax (PBT)** and converts it to cash flows from operating activities.



*We start with *Profit Before Tax* because IAS 7 requires operating cash flows for income tax payments to be reported separately.

CFO – Indirect Method

Intuition behind the approach

Profit Before Tax (PBT)		<i>Our starting point ↪ accrual basis</i>
A	+ Depreciation & Amortization	<i>No cash involved in these expenses. Therefore, we <u>add</u> it back to PBT.</i>
B	- Increase in Noncash Current Assets / + Decrease in Noncash Current Assets	<i>Increase in non-cash assets represent revenues which we did not get cash (e.g. Accounts Receivable). OR the use of cash that still have not been expensed (e.g. Inventory). Therefore, we <u>subtract</u> it from PBT. For decrease, we <u>add</u> it back to PBT.</i>
B	+ Increase in Current Liabilities/ - Decrease in Current Liabilities	<i>Increase in current liabilities represent expenses that did not use cash, so we <u>add</u> it back to PBT. For decrease, we <u>subtract</u> from PBT.</i>
C	- Gain / + Loss on disposal of long-term assets	<i>Because gain & loss from sale of assets are reported under the Investing section, we have to adjust them to avoid double counting. Therefore Gain is <u>subtracted</u>, and Loss is <u>added</u> back into PBT.</i>
D	- Income Taxes paid + Interest expense - interest income - Dividend income	<i>IFRS requires cash for taxes paid on income to be separately disclosed. Taxes paid is a cash outflow so it is <u>subtracted</u> from PBT. Interest paid/received and dividends received needs to also be reported separately.</i>
= Cash Flow from Operations (CFO) ↪ cash basis		

IN CLASS ACTIVITY : RizzTea

Preparing the Statement of Cash Flows (Indirect Method)

Prepare the **Statement of Cash Flows** for Rizz Tea Company for the year 2025 using the ***Indirect Method*** for CFO.

- Use the following to help in the preparation of the SCF:
 - (1) 2024 & 2025 Statement of Financial Position (SFP)
 - (2) 2025 Income Statement (IS)
 - (3) Additional Information:
 - a) The company purchased some new PPE in cash.
 - b) The company disposed \$30,000 worth of PPE with accumulated depreciation of \$26,491. It received some cash for the disposal.
 - c) The company issued ordinary shares, which was settled in cash.
 - d) The company declared dividends, which was settled fully in cash.



IN CLASS ACTIVITY : Rizz Tea

2024 and 2025 SFP & 2025 IS

Rizz Tea Company Statement of Financial Position As at Dec 31, 2024 & 2025		
	2025	2024
ASSETS		
Current assets:		
Cash & cash equivalents	\$ 84,140	\$ 54,497
Accounts Receivable	53,735	49,186
Inventories	39,612	38,754
Interest Receivable	450	-
Prepaid expenses	5,552	12,009
Total current assets	183,489	154,446
PPE	80,000	100,000
Less Accumulated Depreciation	(619)	(18,219)
Total assets	\$ 262,870	\$ 236,227
LIABILITIES & STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 48,005	\$ 49,803
Income tax payable	15,000	12,000
Accrued expenses	29,403	29,799
Total current liabilities	92,408	91,602
Shareholders' Equity:		
Share Capital	9,803	9,158
Retained earnings	160,659	135,467
Total shareholders' equity	170,462	144,625
Total liabilities & shareholders' equity	\$ 262,870	\$ 236,227

Rizz Tea Company Income Statement For the Year Ended Dec 31, 2025	
	2025
Net sales	\$ 585,677
Cost of sales	(405,322)
Gross profit	180,355
Operating expenses:	
Selling, general and administrative	(123,027)
Depreciation expense	(8,891)
Total operating expenses	(131,918)
Operating income	48,437
Other Loss (on disposal of assets)	(2,500)
Interest income	860
Profit before tax	46,797
Income taxes	(14,055)
Net income	32,742



IN CLASS ACTIVITY : Rizz Tea

Preparing the CFO Section

Steps in preparing the SCF – CFO Section:

Step 1:

Use the comparative SFP to calculate the accounts changes for each items in the SFP.

Step 2:

Take the Profit Before Tax from the IS to begin the SCF.

Step 3:

Prepare the CFO section.



IN CLASS ACTIVITY : Rizz Tea

We will be going through in detail
how to create the

Statement of Cash Flows

for the Rizz Tea together
in the lecture using Excel.

(Excel worksheet is available on Canvas)



IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 1

Rizz Tea Company Statement of Financial Position As at Dec 31, 2024 & 2025			STEP 1 : Determine account changes	
	2025	2024	Account Changes	SCF Section
ASSETS				
Current assets:				
Cash & cash equivalents	\$ 84,140	\$ 54,497	29,643	
Accounts Receivable	53,735	49,186	4,549	CFO
Inventories	39,612	38,754	858	CFO
Interest Receivable	450	-	450	CFO
Prepaid expenses	5,552	12,009	-6,457	CFO
Total current assets	183,489	154,446		
PPE	80,000	100,000	-20,000	CFI
Less Accumulated Depreciation	(619)	(18,219)	17,600	CFI
Total assets	\$ 262,870	\$ 236,227		
LIABILITIES & STOCKHOLDERS' EQUITY				
Current liabilities:				
Accounts payable	\$ 48,005	\$ 49,803	-1,798	CFO
Income tax payable	15,000	12,000	3,000	CFO
Accrued expenses	29,403	29,799	-396	CFO
Total current liabilities	92,408	91,602		
Shareholders' Equity:				
Share Capital	9,803	9,158	645	CFF
Retained earnings	160,659	135,467	25,192	
Total shareholders' equity	170,462	144,625		
Total liabilities & shareholders' equity	\$ 262,870	\$ 236,227		

Step 1: Use the comparative SFP to calculate the accounts changes for each items in the SFP.

- Indicate which ones are going to CFO, CFI and CFF of the SCF.

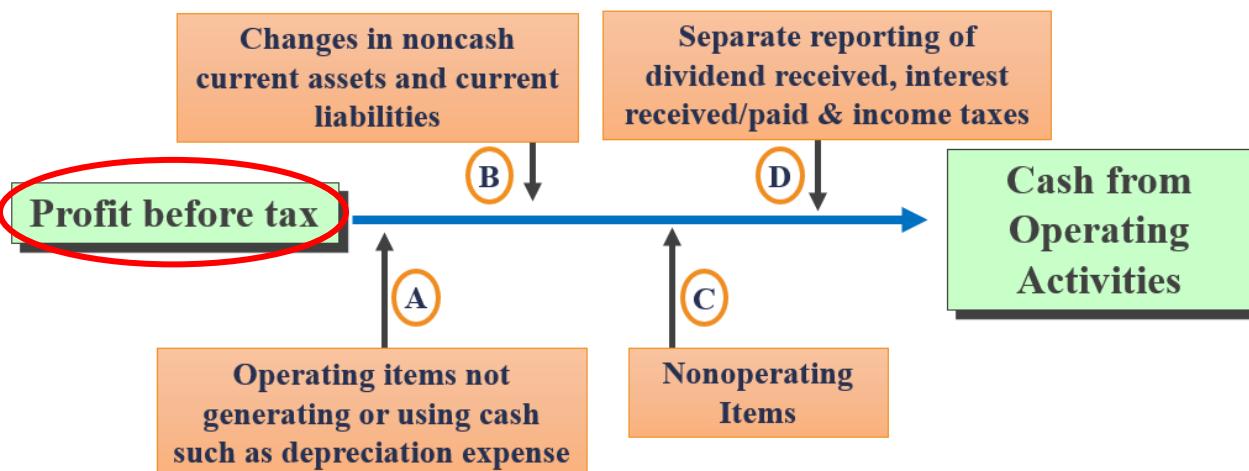


IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 2

Rizz Tea Company Income Statement For the Year Ended Dec 31, 2025		2025
Net sales		\$ 585,677
Cost of sales		(405,322)
Gross profit		180,355
Operating expenses:		
Selling, general and administrative		(123,027)
Depreciation expense		(8,891)
Total operating expenses		(131,918)
Operating income		48,437
Other Loss (on disposal of assets)		(2,500)
Interest income		860
Profit before tax		46,797
Income taxes		(14,055)
Net income		32,742

Step 2: Take the Profit Before Tax from the IS to begin the SCF.



Note: We do not start with Net Income because we will be reporting the cash flow from income taxes separately (see part D), so instead we start our CFO section with PBT.

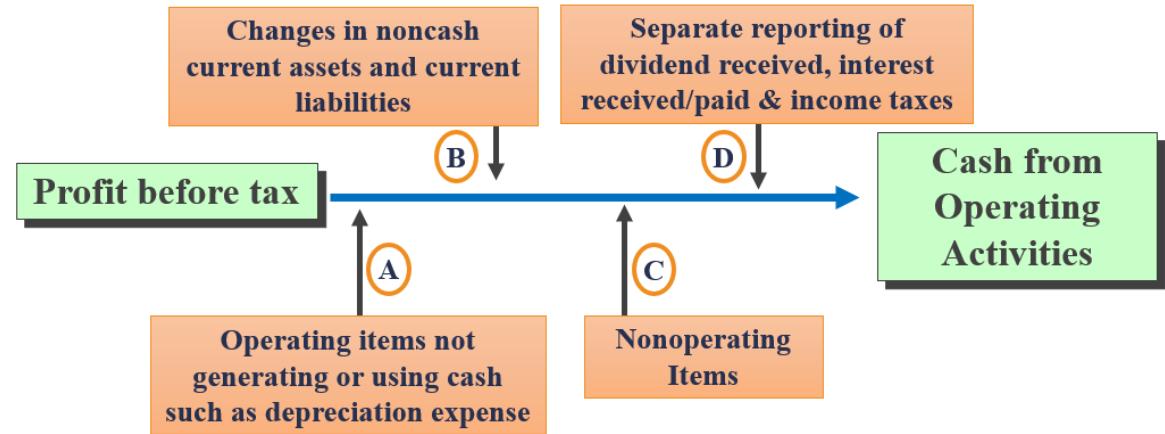


IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 3

Rizz Tea Company Statement of Cash Flows For the Year Ended Dec 31, 2025	
Cash Flows from Operating Activities:	
Profit before taxes	46,797 ←
Adjustments to reconcile profit to net cash from operating activities:	
Depreciation Expense	8,891 ↑
Rizz Tea Company Income Statement For the Year Ended Dec 31, 2025	
	2025
Net sales	\$ 585,677
Cost of sales	(405,322)
Gross profit	180,355
Operating expenses:	
Selling, general and administrative	(123,027)
Depreciation expense	(8,891) ↓
Total operating expenses	(131,918)
Operating income	48,437
Other Loss (on disposal of assets)	(2,500)
Interest income	860
Profit before tax	46,797 ↓
Income taxes	(14,055)
Net income	32,742

Step 3: Prepare the CFO section.



A Adjust for depreciation.



IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 3 (continued)

Rizz Tea Company Statement of Cash Flows For the Year Ended Dec 31, 2025		
Cash Flows from Operating Activities:		
Profit before taxes		
	46,797	
Adjustments to reconcile profit to net cash from operating activities:		
Depreciation Expense	8,891	
Changes in non cash current assets & liabilities:		
Accounts Receivable	(4,549)	
Inventories	(858)	
Prepaid expenses	6,457	
Accounts payable	(1,798)	
Accrued expenses	(396)	

SFP:

ASSETS			Change in Account Balance During Year		
			Increase	Decrease	
Current assets:					
Cash & cash equivalents	\$ 84,140	\$ 54,497	29,643		
Accounts Receivable	53,735	49,186	4,549	CFO	
Inventories	39,612	38,754	858	CFO	
Interest Receivable	450	-	450	CFO	
Prepaid expenses	5,552	12,009	-6,457	CFO	
Current liabilities:					
Accounts payable	\$ 48,005	\$ 49,803	-1,798	CFO	
Income tax payable	15,000	12,000	3,000	CFO	
Accrued expenses	29,403	29,799	-396	CFO	

Step 3: Prepare the CFO section.

B Adjust for changes in noncash current assets and current liabilities

- Use the **worksheet from Step 1** for the changes in accounts
- Use the summary table below to help you remember how to adjust.

Change in Account Balance During Year		
	Increase	Decrease
Noncash Current Assets	Subtract from profit	Add to profit
Current Liabilities	Add to profit	Subtract from profit

IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 3 (continued)

Rizz Tea Company	
Statement of Cash Flows	
For the Year Ended Dec 31, 2025	
Cash Flows from Operating Activities:	
Profit before taxes	46,797
Adjustments to reconcile profit to net cash from operating activities:	
Depreciation Expense	8,891
Changes in non cash current assets & liabilities:	
Accounts Receivable	(4,549)
Inventories	(858)
Prepaid expenses	6,457
Accounts payable	(1,798)
Accrued expenses	(396)
Loss on disposal of asset	2,500
	48,437
	(2,500)
	860
	46,797
	(14,055)
	32,742

IS:

Operating income	48,437
Other Loss (on disposal of assets)	(2,500)
Interest income	860
Profit before tax	46,797
Income taxes	(14,055)
Net income	32,742

Step 3: Prepare the CFO section.

- C** Adjust non-operating items (as they don't belong in the CFO)
 - Loss on disposal of asset is not part of operating activities, it is an investing activity. So the \$2,500 loss is added back in the CFO section as it will be taken into account later in CFI.



IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 3 (continued)

SFP:

ASSETS	
Current assets:	
Cash & cash equivalents	\$ 84,140
Accounts Receivable	53,735
Inventories	39,612
Interest Receivable	450
Prepaid expenses	5,552
Total current assets	183,489
	154,446

IS:	Operating income	48,437
	Other Loss (on disposal of assets)	(2,500)
	Interest income	860
	Profit before tax	46,797
	Income taxes	(14,055)
	Net income	32,742

Step 3: Prepare the CFO section.

D Separate reporting of interest received and paid.

- On SFP, we can see the beginning and ending balance of interest receivable. On IS, interest income for the year is \$860. There is no interest expense for Rizz Tea.
- Use these information to calculate how much interest income was already received in cash this year by analyzing the movement of the interest receivable account.

$$\text{Beg int receivable} + \text{int income} - \text{int received} = \text{End int receivable}$$

$$\$0 + \$860 - \text{int received} = \$450$$

$$\rightarrow \text{Interest received} = \$860 - 450 \\ = \$410$$



IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 3 (continued)

SCF:

Rizz Tea Company Statement of Cash Flows For the Year Ended Dec 31, 2025	
Cash Flows from Operating Activities:	
Profit before taxes	46,797
Adjustments to reconcile profit to net cash from operating activities:	
Depreciation Expense	8,891
Changes in non cash current assets & liabilities:	
Accounts Receivable	(4,549)
Inventories	(858)
Prepaid expenses	6,457
Accounts payable	(1,798)
Accrued expenses	(396)
Loss on disposal of asset	2,500
Interest income	(860)
Cash generated from operations	<u>56,184</u>
Income tax paid	(11,055) ⁽¹⁾
Interest income received	410 ⁽²⁾

D

Step 3: Prepare the CFO section.

Separate reporting of interest received and paid.

- On IS, interest income is \$860. This is the accrual basis interest income. So, first we deduct from profit.
- We have calculated (see previous slide) that interest income received during the year is \$410. So, we add this amount back into CFO.



IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 3 (continued)

SFP:

LIABILITIES & STOCKHOLDERS' EQUITY

Current liabilities:

Accounts payable	\$ 48,005	\$ 49,803
Income tax payable	15,000	12,000
Accrued expenses	29,403	29,799
Total current liabilities	92,408	91,602
Shareholders' Equity:		
Share Capital	9,803	9,158
Retained earnings	160,659	135,467
Total shareholders' equity	170,462	144,625
Total liabilities & shareholders' equity	\$ 262,870	\$ 236,227

IS:

Operating income	48,437
Other Loss (on disposal of assets)	(2,500)
Interest income	860
Profit before tax	46,797
Income taxes	(14,055)
Net income	32,742

Step 3: Prepare the CFO section.

D

Separate reporting of income taxes

- On SFP, we can see the beginning and ending balance of income tax payable. On IS, income tax for the year is \$14,055.
- Use these information to calculate how much tax was already paid in cash this year by analyzing the movement of the tax payable account:

$$\text{Beg tax payable} + \text{tax recognized} - \text{tax paid} = \text{End tax payable}$$

$$\$12,000 + 14,055 - \text{tax paid} = \$15,000$$

$$\rightarrow \text{Tax paid} = \$12,000 + 14,055 - \$15,000$$

$$= \$11,055$$



IN CLASS ACTIVITY : Rizz Tea

CFO Answer Solution – Step 3 (continued)

Rizz Tea Company Statement of Cash Flows For the Year Ended Dec 31, 2025	
Cash Flows from Operating Activities:	
Profit before taxes	46,797
Adjustments to reconcile profit to net cash from operating activities:	
Depreciation Expense	8,891
Changes in non cash current assets & liabilities:	
Accounts Receivable	(4,549)
Inventories	(858)
Prepaid expenses	6,457
Accounts payable	(1,798)
Accrued expenses	(396)
Loss on disposal of asset	2,500
Interest income	(860)
Cash generated from operations	56,184
Income tax paid	(11,055) ⁽¹⁾
Interest income received	410 ⁽²⁾
Net cash from operating activities	45,539

Step 3: Prepare the CFO section.

Separate reporting of income taxes

- Taxes paid in cash is \$11,055.

→ And finally, calculate the
“Net cash from operating activities”



#1. CFO – Indirect Method

Noncash Current Assets & Current Liabilities Adjustments

Use this summary table to help you

Adjusting Profit to CFO:

Change in Account Balance During Year		
	Increase	Decrease
Noncash Current Assets	Subtract from profit	Add to profit
Current Liabilities	Add to profit	Subtract from profit

- If a current asset account has increased, the increase would be subtracted from NI. (e.g. End bal \$50k – Beg bal \$30k = \$20k to be subtracted from NI)
- If current asset account has decreased however, the decrease would be added to NI. (e.g. End bal \$20k – Beg bal \$30k = - \$10k. Subtracting a negative amount will result in an addition to NI)
- For liabilities, increases are added to and decreases are subtracted from NI

Analyzing & Interpreting CFO

- CFO focuses attention on the firm's ability to generate cash internally through operations and its management of current assets and current liabilities (also called working capital)
- CFO is regarded as the most important section of the SCF
- Operations is the company's major source of cash!
- A common rule of thumb followed by financial and credit analysts is to avoid firms with rising net income but falling cash flow from operations.

Investors will not invest in a company if they do not believe that cash generated from operations will be available to pay them dividends or expand the company.

Creditors will not lend money if they do not believe that cash generated from operations will be available to pay back the loan.

#2. Cash Flows from Investing Activities (CFI)

Preparing the CFI

A three-stage process to determine cash provided or used in investing activities:

**Identify changes in
INVESTING-related
accounts**

**Explain these
changes using
reconstruction
analysis**

**Report their cash
flow effects**

IN CLASS ACTIVITY : Rizz Tea

Preparing the CFI Section

Steps in preparing the SCF – CFI Section:

Step 1:

Use the comparative SFP to calculate the accounts changes for CFI items in the SFP

Step 2:

Complete the CFI section using the additional information on investing activities (e.g. purchase/sale of fixed assets, purchase/sale of investments).

Additional Information on Rizz Tea:

- a) The company purchased some new PPE in cash.
- b) The company disposed \$30,000 worth of PPE with accumulated depreciation of \$26,491. It received some cash for the disposal.



IN CLASS ACTIVITY : Rizz Tea

CFI Answer Solution – Step 1

Rizz Tea Company Statement of Financial Position As at Dec 31, 2024 & 2025			STEP 1 : Determine account changes	
	2025	2024	Account Changes	SCF Section
ASSETS				
Current assets:				
Cash & cash equivalents	\$ 84,140	\$ 54,497	29,643	
Accounts Receivable	53,735	49,186	4,549	CFO
Inventories	39,612	38,754	858	CFO
Interest Receivable	450	-	450	CFO
Prepaid expenses	5,552	12,009	-6,457	CFO
Total current assets	183,489	154,446		
PPE	80,000	100,000	-20,000	CFI
Less Accumulated Depreciation	(619)	(18,219)	17,600	CFI
Total assets	\$ 262,870	\$ 236,227		
LIABILITIES & STOCKHOLDERS' EQUITY				
Current liabilities:				
Accounts payable	\$ 48,005	\$ 49,803	-1,798	CFO
Income tax payable	15,000	12,000	3,000	CFO
Accrued expenses	29,403	29,799	-396	CFO
Total current liabilities	92,408	91,602		
Shareholders' Equity:				
Share Capital	9,803	9,158	645	CFF
Retained earnings	160,659	135,467	25,192	
Total shareholders' equity	170,462	144,625		
Total liabilities & shareholders' equity	\$ 262,870	\$ 236,227		

Step 1: Use the comparative SFP to calculate the accounts changes for CFI items in the SFP.

- Just the account changes alone from the SFP is insufficient to inform us of the cash paid/received relating to the purchase and disposals of the PPE!



IN CLASS ACTIVITY : Rizz Tea

CFI Answer Solution – Step 2

Step 2: Find the cash paid for PPE purchase & cash received for PPE disposal.

You may need to analyze the account movements to derive certain figures.

- Cash paid for PPE addition: information given indicates that all purchases were in cash.

$$\text{Beg PPE} + \text{Purchases} - \text{Disposals} = \text{End PPE}$$

$$\$100,000 + \text{Purchases} - 30,000 = \$80,000$$

$$\begin{aligned}\rightarrow \text{Cash paid for purchases} &= \$80,000 + \$30,000 - \$100,000 \\ &= \$10,000\end{aligned}$$

- Cash received for PPE disposal: use the given information to calculate cash received.

Loss on disposal of asset (from IS)	(2,500)
Cost of disposed PPE	30,000
Accum Depr of disposed PPE	<u>(26,491)</u>
NBV of disposed PPE	<u>3,509</u>
→ Cash received on disposal of PPE	<u>1,009</u>



IN CLASS ACTIVITY : Rizz Tea

SCF – CFO & CFI

Rizz Tea Company Statement of Cash Flows For the Year Ended Dec 31, 2025	
Cash Flows from Operating Activities:	
Profit before taxes	46,797
Adjustments to reconcile profit to net cash from operating activities:	
Depreciation Expense	8,891
Changes in non cash current assets & liabilities:	
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Loss on disposal of asset	2,500
Interest income	(860)
Cash generated from operations	56,184
Income tax paid	(11,055) ⁽¹⁾
Interest income received	410 ⁽²⁾
Net cash from operating activities	45,539
 Cash Flows from Investing Activities:	
Cash received from disposal of asset	1,009 ⁽³⁾
Cash paid for purchases of asset	(10,000) ⁽³⁾
Net cash from investing activities	(8,991)



#3. Cash Flows from Financing Activities (CFF)

Preparing the CFF

A three-stage process to determine cash provided or used in financing activities:

**Identify changes in
FINANCING-related
accounts**

**Explain these
changes using
reconstruction
analysis**

**Report their cash
flow effects**

IN CLASS ACTIVITY : Rizz Tea

Preparing the CFF Section

Steps in preparing the SCF – CFF Section:

Step 1:

Use the comparative SFP to calculate the accounts changes for CFF items in the SFP

Step 2:

Complete the CFF section using the additional information on financing activities (e.g. sale/repurchase of stock, dividend payments, borrowings)

Additional Information on Rizz Tea:

- c) The company issued ordinary shares, which was settled in cash.
- d) The company declared dividends, which was settled fully in cash.



IN CLASS ACTIVITY : Rizz Tea

CFF Answer Solution – Step 1

Rizz Tea Company Statement of Financial Position As at Dec 31, 2024 & 2025			STEP 1 : Determine account changes	
	2025	2024	Account Changes	SCF Section
ASSETS				
Current assets:				
Cash & cash equivalents	\$ 84,140	\$ 54,497	29,643	
Accounts Receivable	53,735	49,186	4,549	CFO
Inventories	39,612	38,754	858	CFO
Interest Receivable	450	-	450	CFO
Prepaid expenses	5,552	12,009	-6,457	CFO
Total current assets	183,489	154,446	-20,000	CFI
PPE	80,000	100,000		
Less Accumulated Depreciation	(619)	(18,219)	17,600	CFI
Total assets	\$ 262,870	\$ 236,227		
LIABILITIES & STOCKHOLDERS' EQUITY				
Current liabilities:				
Accounts payable	\$ 48,005	\$ 49,803	-1,798	CFO
Income tax payable	15,000	12,000	3,000	CFO
Accrued expenses	29,403	29,799	-396	CFO
Total current liabilities	92,408	91,602		
Shareholders' Equity:				
Share Capital	9,803	9,158	645	CFF
Retained earnings	160,659	135,467	25,192	
Total shareholders' equity	170,462	144,625		
Total liabilities & shareholders' equity	\$ 262,870	\$ 236,227		

Step 1: Use the comparative SFP to calculate the accounts changes for CFF items in the SFP.

- Just the account changes alone from the SFP is insufficient to inform us of the cash paid/received relating to the share capital and the changes in Retained Earnings.



IN CLASS ACTIVITY : Rizz Tea

CFF Answer Solution – Step 2

Step 2: Find the cash paid/received for financing activities.

You may need to analyze the account movements to derive certain figures.

- Cash received for new shares issuance: information given indicates that all new issuance settled in cash.

$$\text{Beg Share Capital} + \text{Issuance} - \text{Retirement} = \text{End Share Capital}$$

$$\$9,158 + \text{Issuance} - 0 = \$9,803$$

$$\text{Issuance} = \$9,803 - \$9,158$$

$$\text{Issuance} = 645$$

→ **Cash from new issuance = \$645**

- Cash paid for dividends: information given indicates all declared dividends was paid in cash.

$$\text{Beg RE} + \text{NI} - \text{Dividends} = \text{End RE}$$

$$\$135,467 + \$32,742 - \text{Dividends} = \$160,659$$

$$\text{Dividends} = \$135,467 + \$32,742 - \$160,659$$

$$\text{Dividends} = \$7,550$$

→ **Cash paid for dividends = \$7,550**



Rizz Tea Company
Statement of Cash Flows
For the Year Ended Dec 31, 2025

Cash Flows from Operating Activities:

Profit before taxes	46,797
Adjustments to reconcile profit to net cash from operating activities:	
Depreciation Expense	8,891
Changes in non cash current assets & liabilities:	
Accounts Receivable	(4,549)
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Accrued expenses	(396)
Loss on disposal of asset	2,500
Interest income	(860)
	<u>56,184</u>
Cash generated from operations	(11,055) ⁽¹⁾
Income tax paid	(410) ⁽²⁾
Interest income received	410
Net cash from operating activities	45,539

Cash Flows from Investing Activities:

Cash received from disposal of asset	1,009 ⁽³⁾
Cash paid for purchases of asset	(10,000) ⁽³⁾
Net cash from investing activities	(8,991)

Cash Flows from Financing Activities:

Cash received from share issuance	645 ⁽⁴⁾
Cash paid for dividends	(7,550) ⁽⁵⁾
Net cash from financing activities	(6,905)

Net increase in cash	29,643
Beginning cash balance	54,497
Ending cash balance	<u>84,140</u>

FINAL STEP: Complete the SCF

- Calculate net increase/decrease in cash for the year: Add up all the net cash from CFO, CFI and CFF.
- Add to the Beginning cash balance → Ending cash balance **MUST** tie to the ending cash balance on the SFP!!



ASSETS		
Current assets:		
Cash & cash equivalents	\$ 84,140	\$ 54,497
Accounts Receivable	53,735	49,186
Inventories	39,612	38,754
Interest Receivable	450	-
Prepaid expenses	5,552	12,009
Total current assets	<u>183,489</u>	<u>154,446</u>

Analyzing & Interpreting CFF

- The long-term growth of a company is normally financed from three sources:
 - Internally generated funds
 - The issuance of stock
 - Money borrowed on a long-term basis.
- The statement of cash flows shows how management has elected to fund its growth.
- From the CFF, one can see a company's capital structure. What kind of financing from external sources is used, whether it is from shareholders or creditors.
- This information is used by analysts who wish to evaluate the capital structure and growth potential of a business.

Using SCF for Decision Making: Identifying Patterns from SCF

	CF from Operating	CF from Investing	CF from Financing	General Explanation
#1	+	+	+	Company is using cash generated from operations, from sale of assets, and from financing to build up a pile of cash—very liquid company—possibly looking for acquisition.
#2	+	-	-	Company is using cash flows generated from operations to buy fixed assets and to pay down debt or pay owners.
#3	+	+	-	Company is using cash from operations and from sale of fixed assets to pay down debt or pay owners.
#4	+	-	+	Company is using cash from operations and from borrowing (or from owner investment) to expand.
#5	-	+	+	Company's operating cash flow problems are covered by sale of fixed assets, by borrowing, or by stockholder contributions. The negative cash flow from operations could cause long-term problems if it persists.
#6	-	-	+	Company is growing rapidly, but has shortfalls in cash flows from operations and from purchase of fixed assets financed by long-term debt or new investment.
#7	-	+	-	Company is financing operating cash flow shortages and payments to creditors and/or stockholders via sale of fixed assets.
#8	-	-	-	Company is using cash reserves to finance operation shortfall and pay long-term creditors and/or investors.

Source: Michael T. Dugan, Benton E. Gup, and William D. Samson, "Teaching the Statement of Cash Flows," *Journal of Accounting Education*, 9 (1991): 36.

Which of
these pattern
can you see
in the FS of
some real
companies?

BERKSHIRE HATHAWAY INC.

Year Ended December
2024 2023

Cash flows from operating activities:			
Net earnings (loss)	\$ 89,561	\$ 97,147	
Adjustments to reconcile net earnings (loss) to operating cash flows:			
Investment (gains) losses	(52,799)	(74,855)	
Depreciation and amortization	12,855	12,486	
Discount accretion on investments, principally U.S. Treasury Bills	(11,349)	(5,510)	
Other	(892)	(513)	
Changes in operating assets and liabilities:			
Unpaid losses and loss adjustment expenses	2,173	2,628	
Deferred charges - retroactive reinsurance	698	375	
Unearned premiums	376	1,854	
Receivables and originated loans	626	(1,949)	
Inventories	591	1,426	
Other assets	(797)	(1,328)	
Other liabilities	(2,288)	2,570	
Income taxes	(8,163)	14,865	
Net cash flows from operating activities	+ 30,592	49,196	
Cash flows from investing activities:			
Purchases of equity securities	(9,237)	(16,462)	
Sales of equity securities	143,359	40,631	
Purchases of U.S. Treasury Bills and fixed maturity securities	(526,842)	(235,007)	
Sales of U.S. Treasury Bills and fixed maturity securities	48,462	52,302	
Redemptions and maturities of U.S. Treasury Bills and fixed maturity securities	353,538	153,201	
Acquisitions of businesses, net of cash acquired	(396)	(8,604)	
Purchases of property, plant and equipment and equipment held for lease	(18,976)	(19,409)	
Other	(195)	685	
Net cash flows from investing activities	- (10,287)	(32,663)	
Cash flows from financing activities:			
Proceeds from borrowings of insurance and other businesses	5,528	2,133	
Repayments of borrowings of insurance and other businesses	(7,796)	(6,027)	
Proceeds from borrowings of railroad, utilities and energy businesses	7,658	5,684	
Repayments of borrowings of railroad, utilities and energy businesses	(4,151)	(5,284)	
Changes in short-term borrowings, net	(3,059)	2,407	
Acquisitions of treasury stock	(2,918)	(9,171)	
Other, principally transactions with noncontrolling interests	(5,622)	(4,147)	
Net cash flows from financing activities	- (10,360)	(14,405)	
Effects of foreign currency exchange rate changes	(212)	116	
Increase (decrease) in cash and cash equivalents and restricted cash	9,733	2,244	
Cash and cash equivalents and restricted cash at the beginning of the year*	38,643	36,399	
Cash and cash equivalents and restricted cash at the end of the year*	\$ 48,376	\$ 38,643	



Cash, cash equivalents, and restricted cash and cash equivalents, beginning balances

Years ended	September 28, 2024	September 30, 2023
\$ 30,737	\$ 24,977	
Operating activities:		
Net income	93,736	96,995
Adjustments to reconcile net income to cash generated by operating activities:		
Depreciation and amortization	11,445	11,519
Share-based compensation expense	11,688	10,833
Other	(2,266)	(2,227)
Changes in operating assets and liabilities:		
Accounts receivable, net	(3,788)	(1,688)
Vendor non-trade receivables	(1,356)	1,271
Inventories	(1,046)	(1,618)
Other current and non-current assets	(11,731)	(5,684)
Accounts payable	6,020	(1,889)
Other current and non-current liabilities	15,552	3,031
Cash generated by operating activities	+ 118,254	110,543
Investing activities:		
Purchases of marketable securities	(48,656)	(29,513)
Proceeds from maturities of marketable securities	51,211	39,686
Proceeds from sales of marketable securities	11,135	5,828
Payments for acquisition of property, plant and equipment	(9,447)	(10,959)
Other	(1,308)	(1,337)
Cash generated by/(used in) investing activities	+ 2,935	3,705
Financing activities:		
Payments for taxes related to net share settlement of equity awards	(5,441)	(5,431)
Payments for dividends and dividend equivalents	(15,234)	(15,025)
Repurchases of common stock	(94,949)	(77,550)
Proceeds from issuance of term debt, net	—	5,228
Repayments of term debt	(9,958)	(11,151)
Proceeds from/(Repayments of) commercial paper, net	3,960	(3,978)
Other	(361)	(581)
Cash used in financing activities	- (121,983)	(108,488)
Increase/(Decrease) in cash, cash equivalents, and restricted cash and cash equivalents	(794)	5,760
Cash, cash equivalents, and restricted cash and cash equivalents, ending balances	\$ 29,943	\$ 30,737

SCF Patterns of Some Real Companies

FY2022

	CF from Operating	CF from Investing	CF from Financing	General Explanation
Cathay Pacific (FY2021), Berkshire Hathaway (FY2021)	#1 + + +			Company is using cash generated from operations, from sale of assets, and from financing to build up a pile of cash—very liquid company—possibly looking for acquisition.
Singapore Airlines (SQ)	#2 + - -			Company is using cash flows generated from operations to buy fixed assets and to pay down debt or pay owners.
Uber	#3 + + -			Company is using cash from operations and from sale of fixed assets to pay down debt or pay owners.
	#4 + - +			Company is using cash from operations and from borrowing (or from owner investment) to expand.
	#5 - + +			Company's operating cash flow problems are covered by sale of fixed assets, by borrowing, or by stockholder contributions. The negative cash flow from operations could cause long-term problems if it persists.
	#6 - - +			Company is growing rapidly, but has shortfalls in cash flows from operations and from purchase of fixed assets financed by long-term debt or new investment.
	#7 - + -			Company is financing operating cash flow shortages and payments to creditors and/or stockholders via sale of fixed assets.
	#8 - - -			Company is using cash reserves to finance operation shortfall and pay long-term creditors and/or investors.

Berkshire Hathaway, Apple, Amazon, Alphabet (Google), Meta (Facebook), Tesla, Tencent, Pfizer, DBS, Cathay Pacific

Grab

Source: Michael T. Dugan, Benton E. Gup, and William D. Samson, "Teaching the Statement of Cash Flows," *Journal of Accounting Education*, 9 (1991): 36.

SCF Patterns of Some Real Companies

FY2023

	CF from Operating	CF from Investing	CF from Financing	General Explanation
#1	+	+	+	Company is using cash generated from operations, from sale of assets, and from financing to build up a pile of cash—very liquid company—possibly looking for acquisition.
#2	+	-	-	Company is using cash flows generated from operations to buy fixed assets and to pay down debt or pay owners.
#3	+	+	-	Company is using cash from operations and from sale of fixed assets to pay down debt or pay owners.
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#7	-	+	-	Company is financing operating cash flow shortages and payments to creditors and/or stockholders via sale of fixed assets.
#8	-	-	-	Company is using cash reserves to finance operation shortfall and pay long-term creditors and/or investors.

Apple, Grab

Tesla

Berkshire Hathaway,
Amazon, Samsung,
Alphabet (Google),
Meta (Facebook),
Nvidia, Uber, SQ,
Cathay Pacific

Source: Michael T. Dugan, Benton E. Gup, and William D. Samson, "Teaching the Statement of Cash Flows," *Journal of Accounting Education*, 9 (1991): 36.

SCF Patterns of Some Real Companies

FY2024

	CF from Operating	CF from Investing	CF from Financing	General Explanation
	#1 + + +			Company is using cash generated from operations, from sale of assets, and from financing to build up a pile of cash—very liquid company—possibly looking for acquisition.
Apple	#2 + - -			Company is using cash flows generated from operations to buy fixed assets and to pay down debt or pay owners.
	#3 + + -			Company is using cash from operations and from sale of fixed assets to pay down debt or pay owners.
	#4 + - +			Company is using cash from operations and from borrowing (or from owner investment) to expand.
Tesla	#5 - + +			Company's operating cash flow problems are covered by sale of fixed assets, by borrowing, or by stockholder contributions. The negative cash flow from operations could cause long-term problems if it persists.
	#6 - - +			Company is growing rapidly, but has shortfalls in cash flows from operations and from purchase of fixed assets financed by long-term debt or new investment.
	#7 - + -			Company is financing operating cash flow shortages and payments to creditors and/or stockholders via sale of fixed assets.
	#8 - - -			Company is using cash reserves to finance operation shortfall and pay long-term creditors and/or investors.

Berkshire Hathaway,
Amazon, Samsung,
Alphabet (Google),
Meta (Facebook),
Nvidia, Uber, SQ,
Cathay Pacific
Grab

Source: Michael T. Dugan, Benton E. Gup, and William D. Samson, "Teaching the Statement of Cash Flows," *Journal of Accounting Education*, 9 (1991): 36.

Take Away for Lecture 11

- Importance of Cash Flows for a company
- Statement of Cash Flow (SCF)
 - Cash Flow from Operations (CFO)
 - Using the Indirect Method
 - Cash Flow from Investing (CFI)
 - Cash Flow from Financing (CFF)
- Analyzing & interpreting SCF



"Just exactly how bad is our cash flow problem?"

FINAL EXAM Reminder!

FINAL Exam is on 27th Nov 2025 (Thursday) @ 5 PM !

- It is a **2 hours** ON-SITE digital exam **@ MPSH 1A** using EXAMPLIFY.
- There is NO remote exam option!
- It is a **comprehensive** exam covering ALL materials covered in the lectures, assigned textbook readings, tutorials and self-study problems.
- It is a **closed-book** exam, consisting of multiple choice questions and problems.
- You are allowed to bring in **ONE A4 size “cheatsheet”, with notes on both-side!**
- You must bring your **LAPTOP**, calculator, ID cards and stationery. No other unauthorized materials will be allowed in the exam venue. You will be given **3 sheets of rough paper** for workings.
- **If you are unable to attend the exam, you will have to file special consideration.**
- Students will be advised if there are any changes to the above exam procedures.

Mock Exams

- I will be posting **THREE** Mock Exams for you to practice on Examplify in Week 13.
- Please ATTEMPT the mock exams to familiarize yourself with the type of exam questions you can expect for the final.
- For the essay questions, please practice typing in your answers into the answer box:
 - Use tab and spacing when you are typing in your answers (e.g. journal entries/financial statements) into the answer box.
 - Do NOT worry too much about formatting when creating financial statements (e.g. trying to line everything up in a column etc..), just focus on getting the content right.
 - For journal entries, to be clear you can also put Dr and Cr in front of your entries.
 - Important note: there is spreadsheet function in Examplify, you can use it to prepare your answers, but you must **COPY & PASTE the tables into the answer box.** **Anything on the spreadsheet will NOT be saved when you submit the exam on Examplify.**
- I will provide further instructions on Canvas.

That's all folks!



LAST lecture next week: Analyzing Financial Statements

Post your questions on Canvas discussion forum.

My email: hanny.kusnadi@nus.edu.sg