

29.7 The bank statement for G Greene for the month of March 19X6 is:

19X6	Dr £	Cr £	Balance £
Mar 1 Balance			5,197 O/D
Mar 8 L Tulloch	122✓		5,319 O/D
Mar 16 Cheque		244✓	5,075 O/D
Mar 20 A Bennett	208✓		5,283 O/D
Mar 21 Cheque		333✓	4,950 O/D
Mar 31 M Turnbull: trader's credit		57✓	4,893 O/D
Mar 31 BKS: standing order	49		4,942 O/D
Mar 31 Bank charges	28		4,970 O/D

The cash book for March 19X6 is:

19X6	Dr £	19X6	Cr £
Mar 16 N Marsh	244✓	Mar 1 Balance b/d	5,197
Mar 21 K Alexander	333✓	Mar 6 L Tulloch	✓122
Mar 31 U Sinclair	160	Mar 30 A Bennett	✓208
Mar 31 Balance c/d	5,280	Mar 30 J Shaw	490
	<u>6,017</u>		<u>6,017</u>

You are to:

- Write the cash book up to date, and
- Draw up a bank reconciliation statement as on 31 March 19X6.

29.8A Following is the cash book (bank columns) of E Flynn for December 19X7:

19X7	Dr £	19X7	Cr £
Dec 6 J Hall	155✓	Dec 1 Balance b/d	3,872
Dec 20 C Walters	189✓	Dec 10 P Wood	206
Dec 31 P Miller	211	Dec 19 M Roberts	✓315
Dec 31 Balance c/d	3,922	Dec 29 P Phillips	84
	<u>4,477</u>		<u>4,477</u>

The bank statement for the month is:

19X7	Dr £	Cr £	Balance £
Dec 1 Balance			3,872 O/D
Dec 6 Cheque		155✓	3,717 O/D
Dec 13 P Wood	206✓		3,923 O/D
Dec 20 Cheque		189✓	3,734 O/D
Dec 22 M Roberts	315✓		4,049 O/D
Dec 30 Mercantile: standing order	200✓		4,249 O/D
Dec 31 K Saunders: trader's credit		180✓	4,069 O/D
Dec 31 Bank charges	65✓		4,134 O/D

You are required to:

- Write the cash book up to date to take the necessary items into account, and
- Draw up a bank reconciliation statement as on 31 December 19X7.

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Control accounts

Objectives

After you have studied this chapter, you should:

- be able to draw up sales ledger control accounts
- be able to draw up purchases ledger control accounts
- know the sources of information for control accounts
- be able to reconcile the purchase ledger and the sales ledger with their respective control accounts

Need for control accounts

When all the accounts were kept in one ledger a trial balance could be drawn up as a test of the arithmetical accuracy of the accounts. It must be remembered that certain errors were not revealed by such a trial balance. If the trial balance totals disagreed, for a small business the books could easily and quickly be checked so as to find the errors.

However, when the firm has grown and the accounting work has been so divided up that there are several or many ledgers, any errors could be very difficult to find. We could have to check every item in every ledger. What is required is a type of trial balance for each ledger, and this requirement is met by the control account. Thus, it is only the ledgers whose control accounts do not balance that need detailed checking to find errors.

Principle of control accounts

The principle on which the control account is based is simple and is as follows. If the opening balance of an account is known, together with information of the additions and deductions entered in the account, the closing balance can be calculated.

Applying this to a complete ledger, the total of opening balances together with the additions and deductions during the period should give the total of closing balances. This can be illustrated by reference to a sales ledger for entries for a month.

Total of opening balances, 1 January 19X6	£
Add Total of entries which have increased the balances	3,000
	<u>9,500</u>
Less Total of entries which have reduced the balances	12,500
Total of closing balances should be	<u>8,000</u>

Bank Statement

19X9	Dr	Cr	Balance
	£	£	£
Dec 1 Balance b/d			1,740
Dec 7 Cheque		88 ✓	1,828
Dec 11 A Dailey	349 ✓		1,479
Dec 20 R Mason	33 ✓		1,446
Dec 22 Cheque		73 ✓	1,519
Dec 31 Credit transfer: J Walters		54 ✓	1,573
Dec 31 Bank charges	22		1,551

29.4A The bank columns in the cash book for June 19X7 and the bank statement for that month for C Grant are as follows:

Cash Book			
19X7	Dr	19X7	Cr
	£		£
Jun 1 Balance b/d	2,379 ×	Jun 5 D Blake	×150
Jun 7 B Green	158 ×	Jun 12 J Gray	×433
Jun 16 A Silver	93 ✓	Jun 16 B Stephens	×88
Jun 28 M Brown	307 ✓	Jun 29 Orange Club	×57 ✓
Jun 30 K Black	624 ×	Jun 30 Balance c/d	2,833
	<u>3,561</u>		<u>3,561</u>

Bank Statement

19X7	Dr	Cr	Balance
	£	£	£
Jun 1 Balance b/d			2,379 ×
Jun 7 Cheque		158 ×	2,537
Jun 8 D Blackness	150 ×		2,387
Jun 16 Cheque		93 ✓	2,480
Jun 17 J Gray	433 ×		2,047
Jun 18 B Stephens	88 ×		1,959
Jun 28 Cheque		307 ✓	2,266
Jun 29 UDT standing order	44 ×		2,222
Jun 30 Johnson: trader's credit		90 ×	2,312
Jun 30 Bank charges	70 ✓		2,242

You are required to:

- Write the cash book up to date to take the above into account, and then
- Draw up a bank reconciliation statement as on 30 June 19X7.

29.5 Read the following and answer the questions below.

On 31 December 19X8 the bank column of C Tench's cash book showed a debit balance of £1,500.

The monthly bank statement written up to 31 December 19X8 showed a credit balance of £2,950.

On checking the cash book with the bank statement it was discovered that the following transactions had not been entered in the cash book:

✓ Dividends of £240 had been paid directly to the bank.

A credit transfer – Customs and Excise VAT refund of £260 – had been collected by the bank. Bank charges £30.

A direct debit of £70 for the RAC subscription had been paid by the bank.

A standing order of £200 for C Tench's loan repayment had been paid by the bank.

C Tench's deposit account balance of £1,400 was transferred into his bank current account.

A further check revealed the following items:

Two cheques drawn in favour of T Cod £250 and F Haddock £290 had been entered in the cash book but had not been presented for payment.

Cash and cheques amounting to £690 had been paid into the bank on 31 December 19X8 but were not credited by the bank until 2 January 19X9.

- Starting with the debit balance of £1,500, bring the cash book (bank columns) up to date and then balance the bank account.
- Prepare a bank reconciliation statement as at 31 December 19X8.

(Midland Examining Group: GCSE)

29.6A In the draft accounts for the year ended 31 October 19X9 of Thomas P Lee, garage proprietor, the balance at bank according to the cash book was £894.68 in hand.

Subsequently the following discoveries were made:

- Cheque number 176276 dated 3 September 19X9 for £310.84 in favour of G Lowe Limited has been correctly recorded in the bank statement, but included in the cash book payments as £301.84.
- Bank commission charged of £169.56 and bank interest charged of £109.10 have been entered in the bank statement on 23 October 19X9, but not included in the cash book.
- The recently received bank statement shows that a cheque for £29.31 received from T Andrews and credited in the bank statements on 9 October 19X9 has now been dishonoured and debited in the bank statement on 26 October 19X9. The only entry in the cash book for this cheque records its receipt on 8 October 19X9.
- Cheque number 177145 for £15.10 has been recorded twice as a credit in the cash book.
- Amounts received in the last few days of October 19X9 totalling £1,895.60 and recorded in the cash book have not been included in the bank statements until 2 November 19X9.
- Cheques paid according to the cash book during October 19X9 and totalling £395.80 were not presented for payment to the bank until November 19X9.
- Traders' credits totalling £210.10 have been credited in the bank statement on 26 October 19X9, but not yet recorded in the cash book.
- A standing order payment of £15.00 on 17 October 19X9 to Countryside Publications has been recorded in the bank statement but is not mentioned in the cash book.

Required:

- Prepare a computation of the balance at bank to be included in Thomas P Lee's balance sheet as at 31 October 19X9.
- Prepare a bank reconciliation statement as at 31 October 19X9 for Thomas P Lee.
- Briefly explain why it is necessary to prepare bank reconciliation statements at accounting year ends.

(Association of Accounting Technicians)

King simply did not have sufficient funds in his bank account. Suppose he had previously a balance of only £2,000 and yet he has given us a cheque for £5,000. His bank has not allowed him to have an overdraft. In such a case the cheque would be dishonoured. The bank would write on the cheque 'refer to drawer', and we would have to get in touch with King to see what he was going to do about it.

In all of these cases the bank would show the original banking as being cancelled by showing the cheque paid out of our bank account. As soon as this happens they will notify us. We will then also show the cheque as being cancelled by a credit in the cash book. We will then debit that amount to King's account.

When King originally paid his account our records would have appeared as:

K King			
19X9	£	19X9	£
May 1 Balance b/d	<u>5,000</u>	May 20 Bank	<u>5,000</u>

Bank Account			
19X9	£		
May 20 K King	<u>5,000</u>		

After our recording the dishonour, the records will appear as:

K King			
19X9	£	19X9	£
May 1 Balance b/d	<u>5,000</u>	May 20 Bank	<u>5,000</u>
May 25 Bank: cheque dishonoured	5,000		

Bank Account			
19X9	£	19X9	£
May 20 K King	<u>5,000</u>	May 25 K King: cheque dishonoured	<u>5,000</u>

In other words King is once again shown as owing us £5,000.

New terms

Bank Giro credit (p. 280): An amount paid by someone direct into our bank account.

Bank reconciliation statement (p. 281): A calculation comparing the cash book balance with the bank statement balance.

Direct debits (p. 282): Where we give permission for an organisation to collect amounts owing direct from our account.

Dishonoured cheque (p. 283): A cheque which is found to be worth nothing.

Standing order (p. 282): Instructions to our bank to pay specified amounts at given dates.

Unpresented cheque (p. 281): A cheque which has been sent but has not yet gone through the bank account of the receiver of it.

Main points to remember

- 1 A bank reconciliation statement should show whether or not errors have been made either in the bank columns of the cash book or on the bank statement.
- 2 It is best to update the cash book before attempting a bank reconciliation.
- 3 In the case of bank overdrafts, the reconciliation statements show adjustments that are the opposite to those shown with positive bank balances.

Review questions

29.1 From the following draw up a bank reconciliation statement from details as on 31 December 19X6:

Cash at bank as per bank column of the cash book ✓	£ 678 ✓
Unpresented cheques	256 ✓
Cheques received and paid into the bank, but not yet entered on the bank statement ✓	115 ✓
Credit transfers entered as banked on the bank statement but not entered in the cash book	56 ✓
Cash at bank as per bank statement	875 ✓

29.2A Draw up a bank reconciliation statement, after writing the cash book up to date, ascertaining the balance on the bank statement, from the following as on 31 March 19X9:

Cash at bank as per bank column of the cash book (Dr)	£ 3,896 ✓
Bankings made but not yet entered on bank statement	606 ✓
Bank charges on bank statement but not yet in cash book ✓	28 ✓
Unpresented cheques C. Clarke ✓	117 ✓
Standing order to ABC Ltd entered on bank statement, but not in cash book	55 ✓
Credit transfer from A. Wood entered on bank statement, but not yet in cash book	189 ✓

29.3 The following are extracts from the cash book and the bank statement of J. Roche. You are required to:

- (a) Write the cash book up to date, and state the new balance as on 31 December 19X9, and
- (b) Draw up a bank reconciliation statement as on 31 December 19X9.

Cash Book					
19X9	Dr	£	19X9	Cr	£
Dec 1	Balance b/d	1,740	Dec 8	A Dailey	349✓
Dec 7	T J Masters	88✓	Dec 15	R Mason	33✓
Dec 22	J Ellis	73✓	✓Dec 28	G Small	115✓
Dec 31	K Wood	249	Dec 31	Balance c/d	1,831
Dec 31	M Barrett	178			
		<u>2,328</u>			<u>2,328</u>

32.6 Suspense accounts: businesses and examinations

Businesses

Every attempt should be made to find errors. A suspense account should be opened only if all other efforts have failed.

Examinations

Unless it is part of a question, *do not* make your balance sheet totals agree by using a suspense account. The same applies to trial balances. Examiners are very likely to penalise you for showing a suspense account when it should not be required.

New term

Suspense account (p. 309): Account showing balance equal to difference in trial balance.

Main points to remember

- 1 Some of the errors made, but not all, will mean that the profits originally calculated were incorrect.
- 2 Errors that do not affect profit calculations will have an effect only on items in the balance sheet.

Multiple-choice questions

Now attempt Set No 4, consisting of 20 questions, shown on pp. 578–81.

Review questions

32.1 Your bookkeeper extracted a trial balance on 31 December 19X8 which failed to agree by £330, a shortage on the credit side of the trial balance. A suspense account was opened for the difference.

In January 19X9 the following errors made in 19X8 were found:

- (i) Sales day book had been undercast by £100.
- (ii) Sales of £250 to J Cantrell had been debited in error to J Cochrane's account.
- (iii) Rent account had been undercast by £70.
- (iv) Discounts Received account had been undercast by £300.
- (v) The sale of a motor vehicle at book value had been credited in error to Sales account £360.

You are required to:

- (a) Show the journal entries necessary to correct the errors.
- (b) Draw up the suspense account after the errors described have been corrected.
- (c) If the net profit had previously been calculated at £7,900 for the year ended 31 December 19X8, show the calculations of the corrected net profit.

32.2A You have extracted a trial balance and drawn up accounts for the year ended 31 December 19X6. There was a shortage of £292 on the credit side of the trial balance, a suspense account being opened for that amount.

During 19X7 the following errors made in 19X6 were located:

- (i) £55 received from sales of old office equipment has been entered in the sales account.
- (ii) Purchases day book had been overcast by £60.
- (iii) A private purchase of £115 had been included in the business purchases.
- (iv) Bank charges £38 entered in the cash book have not been posted to the bank charges account.
- (v) A sale of goods to B Cross £690 was correctly entered in the sales book but entered in the personal account as £960.

Required:

- (a) Show the requisite journal entries to correct the errors.
- (b) Write up the suspense account showing the correction of the errors.
- (c) The net profit originally calculated for 19X6 was £11,370. Show your calculation of the correct figure.

32.3 Show how each of the following errors would affect trial balance agreement:

- (i) Equipment repairs £720 was debited to the equipment account.
- (ii) £1,700 discounts allowed credited to discounts received account.
- (iii) Stock at close overvalued by £2,000.
- (iv) £750 commission received was debited to the sales account.
- (v) Drawings £305 credited to the capital account.
- (vi) Cheque paying £170 to C Charles entered in cash book but not in personal account.
- (vii) Cheque £248 from L Barnes credited to L Barrett.

Format should be as follows:

Item	If no effect state 'No'	Debit side exceeds credit side by amount shown	Credit side exceeds debit side by amount shown
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(i)

(ii)

(iii)

(iv)

(v)

(vi)

(vii)

32.4 The following is a trial balance which has been incorrectly drawn up:

Trial Balance – 31 January 19X9

	£	£
Capital 1 February 19X8	5,500	
Drawings	2,800	
Stock 1 February 19X8		2,597
Trade debtors		2,130
Furniture and fittings	1,750	
Cash in hand	1,020	
Trade creditors		2,735
Sales		7,430
Returns inwards		85
Discount received	46	
Business expenses	950	
Purchases	4,380	
	<u>16,446</u>	<u>14,977</u>

In addition to the mistakes evident above, the following errors were also discovered:

- 1 A payment of £75 made to a creditor had not been posted from the cash book into the purchases ledger.
- 2 A cheque for £56 received from a customer had been correctly entered in the cash book but posted to the customer's account as £50.
- 3 A purchase of fittings £120 had been included in the purchases account.
- 4 The total of the discounts allowed column in the cash book of £38 had not been posted into the general ledger.
- 5 A page of the sales day book was correctly totalled as £564 but carried forward as £456.

Show the trial balance as it would appear after all the errors had been corrected. You are required to show all workings.

32.5 Study the following and answer the questions below.

The trial balance of Mary Harris (Gowns) as at 31 December 19X8 showed a difference which was posted to a suspense account. Draft final accounts for the year ended 31 December 19X8 were prepared showing a net profit of £47,240. The following errors were subsequently discovered:

- Sales of £450 to C Thomas had been debited to Thomasson Manufacturing Ltd.
- A payment of £275 for telephone charges had been entered on the debit side of the Telephone account as £375.
- The sales journal had been undercast by £2,000.
- Repairs to a machine, amounting to £390, had been charged to Machinery account.
- A cheque for £1,500, being rent received from Atlas Ltd, had only been entered in the cash book.
- Purchases from P Brooks, amounting to £765, had been received on 31 December 19X8 and included in the closing stock at that date, but the invoice had not been entered in the purchases journal.

Questions

- (i) Give the journal entries, without narratives, necessary to correct the above errors.
- (ii) Show the effect of each of these adjustments on the net profit in the draft accounts and the correct profit for the year ended 31 December 19X8.
- (b) (i) State briefly the purpose of the journal, giving a suitable example of its use.
- (ii) State why it is necessary to distinguish between capital and revenue expenditure.

(Midland Examining Group: GCSE)

32.6A Gail Dawson is the owner of a retail business. She has employed an inexperienced bookkeeper to maintain her accounting records.

- (a) On 31 March 19X9, the end of the business's accounting year, the bookkeeper extracted the following trial balance from the business's records:

Trial Balance at 31 March 19X9

	Dr £	Cr £
Fixed assets at cost	18,300	
Provision for depreciation of fixed assets, 1 April 19X8	2,800	
Stocks 1 April 19X8	3,700	
31 March 19X9		2,960
Trade debtors		1,825
Trade creditors	864	
Balance at bank (overdrawn)	382	
Capital		26,860
Drawings	7,740	
Sales	26,080	
Purchases		18,327
Running expenses	6,904	
Provision for doubtful debts	90	
Suspense		
	<u>£66,860</u>	<u>£66,860</u>

Required:

- 1 A corrected version of Gail Dawson's trial balance dated 31 March 19X9 based on the above information, but with an amended figure for the suspense account.
- (b) The following errors were found in the accounting system after a corrected version of the trial balance above was prepared.
 - (i) The total of the sales day book for December 19X8 had been overstated by £120.
 - (ii) In January 19X9 some new office equipment had been purchased for £360; this had been debited to the purchases account.
 - (iii) A payment by cheque to a creditor, £216, had been entered in the books as £261.
 - (iv) A credit note for £37 sent to a customer had been overlooked.
 - (v) The owner had withdrawn a cheque for £80 for private use in October 19X8; both the bank and drawings account had been credited with this amount.

Required:

In the books of Gail Dawson

- 2 Journal entries to correct each of these errors.
(Note: narratives are NOT required.)
- 3 The suspense account. (Start with the amount in the corrected trial balance given in answer to Required 1 above, and include any entries arising from the correction of the errors.)
- 4 An explanation of the term 'error of commission'. (Give an example of such an error to illustrate your answer.)

(Southern Examining Group: GCSE)

Olwen

31 Sales	7,090	31 Cash	104
Cash refunded	37	Bank	6239
Bank: dishonored cheque	29	Bad debts	306
Interest on debts	50	Discounts allowed	298
Balances c/d	40	Returns inwards	664
		Balances c/d	<u>3,429</u>
	<u>11,062</u>		<u>11,062</u>

Note that you do not set off the debit and credit balances in the sales ledger

Cash Flow Statement - IAS 7

Cash flow statement may provide considerable information about what is really happening in a business beyond that contained in either the income statement or the balance sheet. Analyzing this statement should not present an intimidating task; instead it will quickly become obvious that the benefits of understanding the sources and uses of a company's cash far outweigh the costs of undertaking some very straightforward analyses. Thus, management of cash is very essential. There should be focus on movement of cash and its equivalents. Cash means, cash in hand and demand deposits with the bank. Cash equivalent consists of bank overdraft, cash credit, short term deposits and marketable securities.

Cash Flow Statement deals with flow of cash which includes cash equivalents as well as cash. This statement is additional information to the users of Financial Statements. The statement shows the incoming and outgoing of cash. The statement assesses the capability of the enterprise to generate cash and utilize it. *Thus a Cash-Flow statement may be defined as a summary of receipts and disbursements of cash for a particular period of time. It also explains reasons for the changes in cash position of the firm.*

Cash flows are cash inflows and outflows. Transactions which increase the cash position of the entity are called as inflows of cash and those which decrease the cash position as outflows of cash. Cash flow Statement traces the various sources which bring in cash

Group C&D

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such as cash from operating activities, sale of current and fixed assets, issue of share capital and debentures etc. and applications which cause outflow of cash such as loss from operations, purchase of current and fixed assets, redemption of debentures, preference shares and other long-term debt for cash. In short, a cash flow statement shows the cash receipts and disbursements during a certain period. The statement of cash flow serves a number of objectives which are as follows:

- Cash flow statement aims at highlighting the cash generated from operating activities.
- Cash flow statement **helps in planning the repayment of loan** schedule and replacement of fixed assets, etc.
- Cash is the centre of all financial decisions. It is used as the basis for the projection of future investing and financing plans of the enterprise.
- Cash flow statement helps to ascertain the liquid position of the firm in a better manner. Banks and financial institutions mostly prefer cash flow statement to analyse liquidity of the borrowing firm.
- Cash flow Statement helps in efficient and effective management of cash.
- The management generally looks into cash flow statements to understand the internally generated cash which is best utilised for payment of dividends.

Who cares about a Cash Flow Statement?

- **Executives** want to know if the cash generated by the company will be sufficient to fund their expansion strategy
- **Stockholders** want to know if the firm is generating enough cash to pay dividends
- **Suppliers** want to know if their customers will be able to pay if offered credit
- **Investors** want to evaluate future growth potential
- **Employees** are interested in the overall viability of their employer as indicated by its ability to fund its operations

Format of the Cash Flow Statement

There are two formats of preparing the Cash Flow Statement. However the two yield the same results

The direct method

The direct method shows operating cash receipts and payments, for example, cash paid to suppliers and employees and cash received from customers. This is useful to users as it shows the actual sources and uses of cash. However, many entities will not generate this information as a matter of course and so it may prove expensive to produce.

The indirect method

The indirect method instead starts with profit before taxation, adding back items shown elsewhere on the cash flow statement (e.g. finance cost) and adjusting for non-cash items included in arriving at the operating profit figure. Non-cash items would include the following

- *Depreciation:*

this is a book adjustment to reflect the wearing out of an asset; the cash impact of non-current assets is the buying of the asset.

- *Profits/losses on disposal of non-current assets:*

Profit is not cash – the cash impact of the disposals the disposal proceeds.

- *Changes in inventories:*

Because operating profit is calculated after charging cost of sales, which has been adjusted for opening and closing inventory, we need the figure for total cash spent on materials in the year, not the cost of the goods used in the year.

- *Changes in receivables:*

The figure included in the income statement is the sales revenue – we need the cash received from customers and so we must take account of opening and closing receivables for the year.

- *Changes in payables:*

For the same reason as above – we need to get to the figure for actual cash paid to suppliers. Entities are required to disclose the calculation using the indirect method as it provides the reconciliation of operating profit to cash flows from operating activities, which is an integral part of the cash flow statement (it is therefore more likely to be the indirect method that is requested in examination, but the direct method will occasionally be examined).

- The cash flow statement is divided into three sections:

- o *Cash flow from operating activities:*

Shows the results of cash inflows and outflows related to the fundamental operations of the basic line or lines of business in which the company engages. (Example: cash receipts from the sale of goods or services and cash outflows for purchasing inventory and paying rent and taxes.)

- o *Cash flow from investing activities:*

Associated with purchases and sales of non-current assets (Example: building and equipment purchases or sales of investments or subsidiaries.)

- o *Cash flow from financing activities:*

Associated with financing the firm (Example: selling and paying off bonds and issuing stock and paying dividends)

Examples of cash flows from operating activities are:

- (a) Cash receipts from the sale of goods and the rendering of services;
- (b) Cash receipts from royalties, fees, commissions and other revenue;

(c) Cash payments to suppliers for goods and services;

(d) Cash payments to and on behalf of employees;

(e) Cash receipts and cash payments of an insurance entity for premiums and claims, annuities and other policy benefits;

(f) Cash payments or refunds of income taxes unless they can be specifically identified with financing and investing activities; and

(g) Cash receipts and payments from contracts held for dealing or trading purposes.

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

Investing Activities

<i>Cash inflow</i>	<i>Cash outflow</i>
Sale of fixed assets	Purchase of fixed assets
Sale of investment	Purchase of investment
Interest received	
Dividend received	

Financing Activities

<i>Cash inflows</i>	<i>Cash outflows</i>
Issue of shares	Cash repayments of amounts borrowed
Issue of debentures in cash	Dividends paid on equity and preference share capital
Proceeds from long term/ short term borrowings	Interest paid on loans/debentures

• Exceptions

- o Short-term marketable securities are treated as long-term investments and appear in cash flow from investing activities
- o Short-term debt is treated as long-term debt and appears in cash flow from financing activities
- o Although dividends are handled as a cash outflow in the cash flow from financing activities section, interest payments are considered an operating outflow, despite the fact that both are payments to outsiders for using their money.

Example of a Statement of Cash Flow: notice how it separates the three different cash flow activities

ABC LTD

Statement of Cash Flows

For the year ended 31 December 20xx

Cash Flow from Operating Activities

Net Income	XXX,XXX
<i>Adjustments to reconcile net income to net</i>	
<i>Cash provided by operating activities:</i>	
Depreciation and amortization	XX,XXX
Gain on sale of investment/ASSET	(X,XXX)

Changes in other accounts affecting operations:

(Increase)/decrease in accounts receivable	X,XXX	
(Increase)/decrease in inventories	X,XXX	
(Increase)/decrease in prepaid expenses	X,XXX	
Increase/ (decrease) in accounts payable	X,XXX	
Increase/ (decrease) in taxes payable	X,XXX	
Net cash provided by operating activities	<u>XXX,XXX</u>	XXXXX

Cash Flow from Investing Activities

Capital expenditures	(XXX,XXX)	
Proceeds from sales of equipment	XX,XXX	
Proceeds from sales of investments	XX,XXX	
Investments in subsidiary	(XXX,XXX)	
Net cash provided by investing activities	<u>(XXX,XXX)</u>	XXXX

Cash Flow from Financing Activities

Payments of long-term debt	(XX,XXX)	
Proceeds from issuance of long-term debt	XX,XXX	
Proceeds from issuance of common stock	XXX,XXX	
Dividends paid	(XX,XXX)	
Purchase of treasury stock	(XX,XXX)	
Net cash provided by financing activities	<u>(XX,XXX)</u>	<u>XXXXXX</u>

Increase (Decrease) in Cash XXX,XXX

Cash at the beginning of the period XXX

Cash at the END of the period XXX

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• Operating Activities:

- o The cash flow from operating activities section of a cash flow statement can be presented using the direct format or the indirect format. The bottom line is the same, but the two begin at different points. Companies are free to use either format.

Below is an example of both formats.

o Direct method:

Shows how much cash came in for sales and how much cash went out for inventory and other operating expenditures.

o Indirect method:

Starts with net income as a figure that summarizes most of the cash transactions for operating activities in a firm. However, net income also includes transactions that are not cash, so we must eliminate the non-cash transactions from the net income figure to arrive at an accurate presentation of cash flow from operating activities.