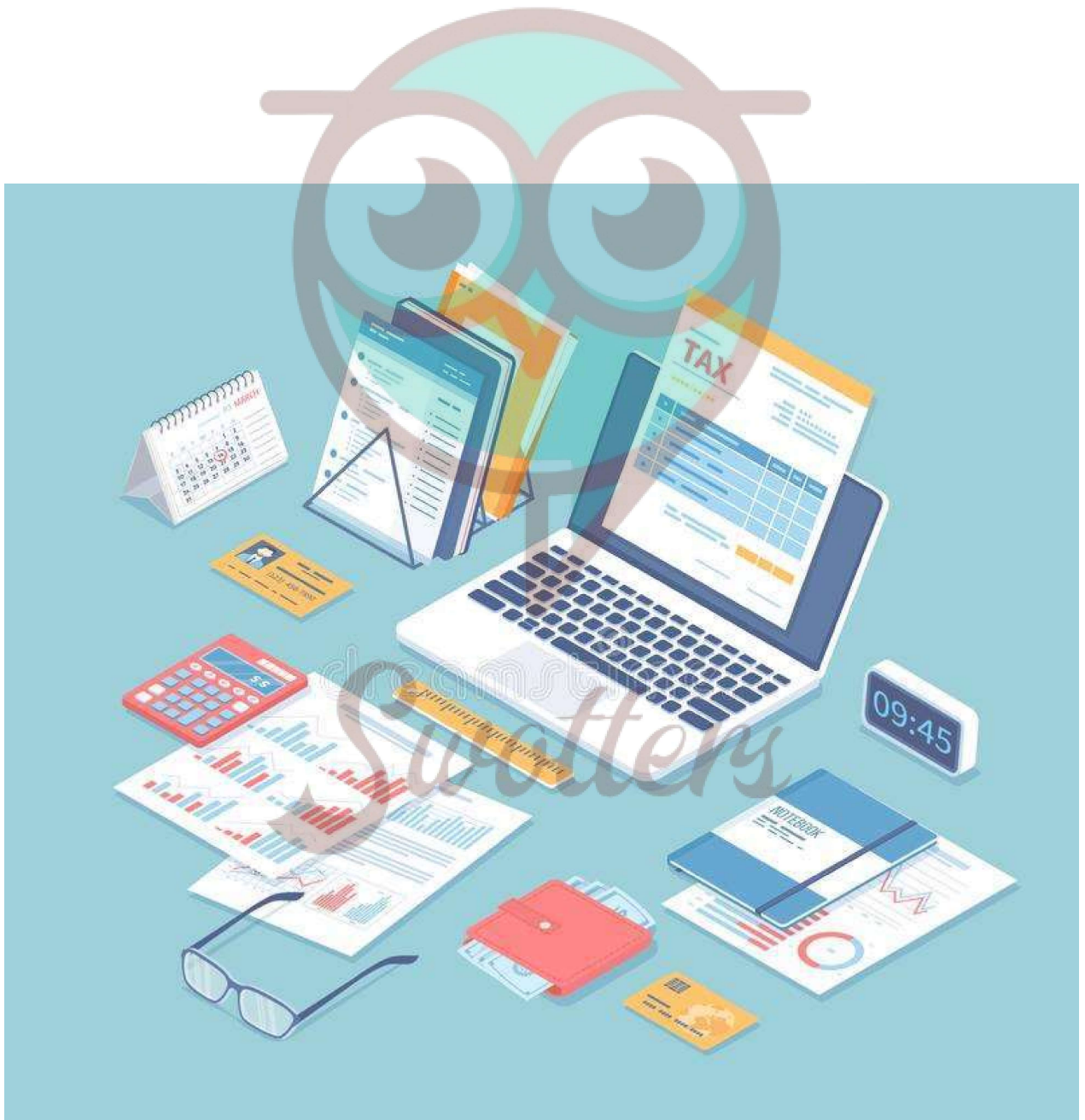


ACCOUNTANCY



Important Questions

Multiple Choice questions-

Question 1. Investments made with the purpose to resell after the expiry of three months will come under which of the following activity?

- (a) Investment
- (b) Financing
- (c) Operating
- (d) Cash equivalents

Question 2. Which of the following is the source of cash?

- (a) Cash deposited into bank
- (b) Cash withdrawn from the bank
- (c) Sale of marketable securities
- (d) Sale of goods for cash costing ₹ 20,000 for ₹ 16,000.

Question 3. While calculating cash flows from operating profit, which of the following is not considered in the net profit?

- (a) Amortisation of goodwill
- (b) Writing off bad debts
- (c) Writing off depreciation
- (d) Interest paid on bank overdraft

Question 4. Which of the following statement is incorrect about cash flow statement?

- (a) It provides information about cash inflows and cash outflows .
- (b) It provides information of flows of cash under three major categories
- (c) It reconciles bank balance with the bank balance as per bank statement
- (d) It helps in preparing cash budget

Question 5. Which of the following will come under operating activity?

- (a) Issue of shares for cash
- (b) Interest received on short-term investments
- (c) Trading commission received by a manufacturing company
- (d) Sale of marketable securities

Question 6. Which of the following will not come under anywhere in cash flow statement?

- (a) Repayment of borrowings
- (b) Issue of bonus shares
- (c) Sale of investments
- (d) Dividend paid

Question 7. A plant whose original cost was ₹ 40,000, accumulated depreciation provided till the date of sale was ₹ 15,000 was sold at 20% above the book value. Cash flow from operating activities will be

- (a) ₹ 48,000

- (b) ₹ 30,000
- (c) ₹ 18,000
- (d) ₹ 25,000

Question 8. Where will you show sale and purchase of shares and securities if it relates to revenue generating activity?

- (a) Cash flow from investment activities
- (b) Cash flows from financing activities
- (c) Cash flows from operating activities
- (d) Cash and cash equivalents

Question 9. Which of the following transaction is always shown under financing activities?

- (a) Interest received on investments
- (b) Interest paid on investments
- (c) Dividend paid
- (d) Dividend received

Question 10. Investments made by a financial enterprise with the purpose to resell after the expiry of three months will come under which of the following activity?

- (a) Investment
- (b) Financing
- (c) Operating
- (d) Cash equivalents

Vezy Short Questions-

1. What is meant by 'Cash Flows'?
2. How will 'commission received' be treated while preparing cash-flow-statement?
3. How is 'dividend paid' treated by a financial enterprise for the purpose of preparing cash flow statement?
4. When can 'Receipt of Dividend' be classified as an operating activity State. Also give reason in support of your answer.
5. What is meant by 'Cash Flow Statement'?
6. What is meant by 'Cash Flows'?
7. How will 'commission received' be treated while preparing a cash-flow-statement?
8. State any one advantage of preparing cash flow statement.

Short Questions-

1. What is a Cash Flow Statement?

2. How are the various activities classified (as per AS-3 revised) while preparing cash flow statement?
3. State the uses of cash flow statement?
4. What are the objectives of preparing cash flow statement?
5. State the meaning of the terms: Cash Equivalents, Cash flows.
6. "The nature/type of enterprise can change altogether the category into which a particular activity may be classified." Do you agree? Illustrate your answer.

Long Questions-

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

MCQ Answers-

1. Answer: (d) Cash equivalents
2. Answer: (d) Sale of goods for cash costing ₹ 20,000 for ₹ 16,000.
3. Answer: (b) Writing off bad debts
4. Answer: (c) It reconciles bank balance with the bank balance as per bank statement
5. Answer: (c) Trading commission received by a manufacturing company
6. Answer: (b) Issue of bonus shares
7. Answer: (b) ₹ 30,000
8. Answer: (c) Cash flows from operating activities
9. Answer: (c) Dividend paid
10. Answer: (c) Operating

Very Short Answers-

1. Answer: Cash Flows imply movement of cash in and out due to some non-cash items.
2. Answer: It will be treated as Cash flows from operating activities.
3. Answer: Dividend paid is treated as a financing activity.
4. Answer: Receipt of dividend can be an operating activity for a financial company as it is a principal revenue generating activity.
5. Answer: A Cash Flow Statement is a statement that provides information about the historical

changes in Cash & Cash Equivalents of an enterprise by classifying cash flows into Operating, Investing and Financing Activities.

6. Answer: Cash Flows imply movement of cash in and out due to some non-cash items.
7. Answer: It will be treated as Cash flows from operating activities.
8. Answer: It helps in short term financial planning.

Short Answers-

1. A financial statement that represents the inflow and outflow of cash and cash equivalents of a company is called a cash flow statement. It shows how well a company can manage its cash position and generates enough cash to pay the obligations in the form of debt and also run the operational expenses.
2. **Three types of activities are defined:**
 - a. Operating Activities.
 - b. Financing Activities.
 - c. Investing Activities.
3. **Following are uses of cash flow statement:**
 - i. Useful for evaluating cash position of a firm.
 - ii. Helpful in finding deficiencies and variations in firms performance which helps in effective decision making.
 - iii. It helps in assessment of liquidity of a company.
 - iv. It analyses cash receipts and payments from the various activities of a company and helps in short term planning.
 - v. It helps in segregating cash flows obtained from the various activities of the business.
 - vi. It helps in providing decision about distribution of profit.
 - vii. It is useful for short term financial analysis.
4. **Following are the objectives:**
 - i. To determine inflow and outflow of cash and the cash equivalents obtained from the different kind of activities.

- ii. To seek out various reasons responsible for change in cash balances during the accounting period.
 - iii. It helps in depicting the position of the company in terms of liquidity and solvency.
 - iv. It also helps in determining the requirement and the corresponding availability of cash for business in future.
5. Cash equivalents are investments that are highly liquid in nature and do not change value easily. Cash equivalents are essential for managing short term cash requirements or any such investments. For example treasury bills.

Cash Flows: It is the inflow and outflow of cash and cash equivalents. Cash inflows boosts cash balance and cash outflow has a negative impact on cash balance.

6. Yes, it can happen. For example, there are two firms one is engaged in real estate and the other in general business. For the firm engaged in real estate sale of building will be regarded as part of operating activity while for the firm dealing with general business, purchase or sale of a building is regarded as an investing activity. Therefore, it can be said that nature and type of enterprise determines the type of activities.

Long Answers-

1. **Following steps are followed:**

- i. Determine cash flows obtained from operating activities.
- ii. Determine cash flows obtained from financing activities.
- iii. Determine cash flow obtained from investing activities.
- iv. Determine net increase or decrease which is obtained by adding amounts from all the cash flow activities.
- v. Add the opening balance of cash and the cash equivalents and deduct the same from the amount determined in the previous step.

There are two methods which are used for preparation of cash flow statement:

1. Direct Method
2. Indirect Method.

Direct Method

Cash Flow Statement

	Particulars	Amount Rs	Amount Rs
A.	Cash Flow from Operating Activities		
	Cash Sales	**	
	Cash receipt from Debtors	**	
	<i>Less:</i> Cash Purchases	**	
	Cash paid to creditors and other expenses	**	
	Cash Generated from Operating Activities	**	
	<i>Less:</i> Income Tax Paid	**	
	Cash flow before Extraordinary Items	**	
	<i>Add/Less:</i> Extraordinary Items	**	
	Net Cash Flow from (used in) Operating Activities	**	**
B.	Cash Flow from Investing Activities	**	
	Sale of Fixed Assets	**	
	Sale of long-term Investments	**	
	Interest Received	**	
	Dividend Received	**	
	Rent Received	**	
	<i>Less:</i> Purchase of Fixed Assets	**	
	<i>Less:</i> Purchase of long-term Investment	**	
	Net Cash Flow from Investing Activities	**	**
C.	Cash Flow from Financing Activities		
	Proceeds from Issue of Shares	**	
	Proceeds from Issue of Debentures and Other Long-term Borrowings	**	
	<i>Less:</i> Repayment of Debentures and Other Long-term Borrowings	**	
	<i>Less:</i> Redemption of Preference Shares	**	
	<i>Less:</i> Interest Paid	**	
	<i>Less:</i> Dividend Paid	**	
	Net Cash flow from Financing Activities	**	**
	Net Increase (or Decrease in Cash and Cash Equivalents (A+B+C))		**
	Cash and Cash Equivalents at the beginning (Cash in Hand, Cash at Bank, Marketable Securities, Short-term Deposits)		**
	Cash and Cash Equivalent at the end		**

Indirect Method

Cash Flow Statement

	Particulars	Amount Rs	Amount Rs
A.	Cash Flow from Operating Activities:		
	Net Profit before tax and extraordinary items		***
	<i>Add:</i> Non-Cash Expenses and non operating expenses.		
	Depreciation	**	
	Goodwill	**	
	Interest paid	**	
	Loss on sale of fixed assets	**	**
	<i>Less:</i> Non-Operating Incomes.		
	Dividend received	**	
	Profit on sale of fixed assets	**	
	Interest received	**	**
	Operating Profit before Working Capital Changes		***
	<i>Add:</i> Decrease in Current Assets	***	
	Increase in Current Liabilities	**	***
	<i>Less:</i> Increase in Current Assets	***	
	Decrease in Current Liabilities	***	***
	Cash generated from Operating Activities		***
	<i>Less:</i> Income tax paid		***
	Cash flow before Extra ordinary items		***
	<i>Add/Less:</i> Extra ordinary items		***
	Net Cash Flow from Operating Activities		***
B.	Cash Flow from Investing Activities	**	
	Sale of Fixed Assets	**	
	Sale of Long-term Investments	**	
	Interest Received	**	
	Dividend Received	**	
	Rent Received	**	
	<i>Less:</i> Purchase of Fixed Assets	**	
	<i>Less:</i> Purchase of long term Investment	**	
	Net Cash Flow from Investing Activities	**	**
C.	Cash Flow from Financing Activities		
	Proceeds from Issue of shares	**	
	Proceeds from Issue of Debentures and other Long-term Borrowings	**	
	<i>Less:</i> Repayment of Debentures and other Long-term Borrowings	**	
	<i>Less:</i> Redemption of preference Share	**	
	<i>Less:</i> Interest paid	**	
	<i>Less:</i> Dividend paid	**	
	Net Cash Flow from Financing Activities	**	**
	Net Increase (or Decrease in Cash and Cash Equivalents (A+B+C))		**
	Cash and Cash Equivalents at the beginning (Cash in Hand, Cash at Bank, Marketable Securities, Short-term Deposits)		**
	Cash and Cash Equivalents at the end		**

Note: Preparation of Cash Flow Statement using Direct Method has been excluded from the prescribed syllabus. The format is given since the question has not specified the method explicitly. Students can refer to the direct method for the knowledge purpose.

2. In indirect method cash flow statement begins with net income or loss, and thereafter the additions or deductions from that amount for non-cash expense and revenue items, which results in cash flow from operating activities.

Following are some items:

- i. Items that are non-cash in nature like goodwill, depreciation are added towards net profit.
- ii. Expenses that are non-operating in nature like transfer to reserve and loss on sale of fixed assets which are added back to show Net Profit earned.
- iii. Provision such as discount for debtors, doubtful debts, proposed dividends etc. should be added to Net Profit.
- iv. Any decrease in current assets and an increase in current liabilities is added to operating profit.

Following items get deducted from net profit of P & L account:

- i. Incomes that are non-operating in nature like sale of fixed assets.
 - ii. Non-trading incomes like dividend received, tax refund, interest received.
 - iii. Increase in current assets and decrease in current liabilities.
3. Investing activities consist of sales and purchase of fixed assets that are long term in nature, like building, land, furniture and plant and machinery etc. It also includes sale and purchase of items that are not cash equivalents. If any income is received from these assets it is regarded as a part of investing activities.

The major cash inflows and outflows that are involved in investing activities are:

- i. Cash receipts that are obtained when fixed assets are sold off and it includes intangible assets.
- ii. Acquiring fixed assets which also includes intangibles like goodwill using cash payments, the payments is for the research and development and assets that are self-constructed.
- iii. Acquiring shares, debt instruments or warrants using cash payments.

- iv. Disposal of shares and warrants that yield cash receipts.
- v. Loans and cash advances that are made to third parties (does not includes loans and advances made by financial enterprises).
- vi. Cash receipts obtained from any insurance company for a property that is involved in accident.
- vii. Cash receipts that are obtained for repayment of loans and cash advances made to third parties.
- viii. Any type of income that is obtained from fixed assets like interest, dividend and rent (not in case of financial enterprises).

Direct Method

Cash Flow Statement

	Particulars	Amount Rs	Amount Rs
	Net Cash Flow from (used in) Operating Activities	**	**
B.	Cash Flow from Investing Activities	**	
	Sale of Fixed Assets	**	
	Sale of long-term Investments	**	
	Interest Received	**	
	Dividend Received	**	
	Rent Received	**	
	<i>Less:</i> Purchase of Fixed Assets	**	
	<i>Less:</i> Purchase of long-term Investments	**	
	Net Cash Flow from Investing Activities	**	**

Indirect Method

Cash Flow Statement

Particulars	Amount Rs	Amount Rs
Net Cash Flow from Operating Activities		***
Cash Flow from Investing Activities	**	
Sale of Fixed Assets	**	
Sale of Long-term Investments	**	
Interest Received	**	
Dividend Received	**	
Rent Received	**	
<i>Less: Purchase of Fixed Assets</i>	**	
<i>Less: Purchase of long term Investment</i>	**	
Net Cash Flow from Investing Activities	**	**

Note: Preparation of Cash Flow Statement using Direct Method has been excluded from the prescribed syllabus. The format is given since the question has not specified the method explicitly. Students can refer to the direct method for the knowledge purpose.

4. Financing activities are those activities that are related to capital or long term funds of an enterprise. These activities results in the change in the capital and borrowed funds.

As per the AS3, the major cash inflows from financing activities are as follows:

- i. Cash proceeds from issue of shares and other similar instruments.
- ii. Cash proceeds from issue of debentures, loans, notes, bonds, and other short and long-term borrowings.

As per the AS3, the major cash outflows from financing activities are as follows:

- i. Cash repayments of the amount borrowed in form of debentures, loans, notes bonds, and

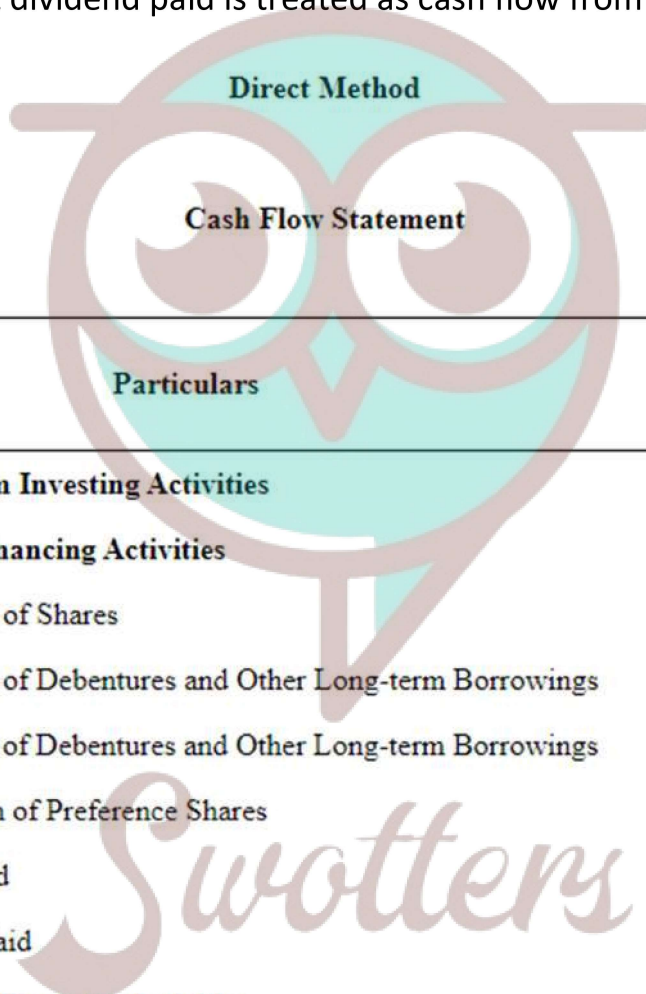
other short and long-term borrowings.

ii. Buy-back of shares and debentures.

iii. Interest paid on debentures, loans, and advances.

iv. Dividend paid to the preference shareholders and equity shareholders.

An important point that must be noted is that the purchase and sale of securities, interest paid or received and dividend received is treated as cash flow from operating activities for an investment company. But dividend paid is treated as cash flow from financing activities.



Particulars	Amount	Amount
	Rs	Rs
Net Cash Flow from Investing Activities	**	**
Cash Flow from Financing Activities		
Proceeds from Issue of Shares	**	
Proceeds from Issue of Debentures and Other Long-term Borrowings	**	
<i>Less:</i> Repayment of Debentures and Other Long-term Borrowings	**	
<i>Less:</i> Redemption of Preference Shares	**	
<i>Less:</i> Interest Paid	**	
<i>Less:</i> Dividend Paid	**	
Net Cash flow from Financing Activities	**	**
Net Increase (or Decrease in Cash and Cash Equivalents (A+B+C))		**
Cash and Cash Equivalents at the beginning (Cash in Hand, Cash at Bank, Marketable Securities, Short-term Deposits)		**
Cash and Cash Equivalent at the end		**

Indirect Method

Cash Flow Statement

Particulars	Amount	Amount
	Rs	Rs
Net Cash Flow from Investing Activities	**	**
Cash Flow from Financing Activities		
Proceeds from Issue of shares	**	
Proceeds from Issue of Debentures and other Long-term Borrowings	**	
<i>Less:</i> Repayment of Debentures and other Long-term Borrowings	**	
<i>Less:</i> Redemption of preference Share	**	
<i>Less:</i> Interest paid	**	
<i>Less:</i> Dividend paid	**	
Net Cash Flow from Financing Activities	**	**
Net Increase (or Decrease in Cash and Cash Equivalents (A+B+C))		**
Cash and Cash Equivalents at the beginning (Cash in Hand, Cash at Bank, Marketable Securities, Short-term Deposits)		**
Cash and Cash Equivalents at the end		**

Note: Preparation of Cash Flow Statement using Direct Method has been excluded from the prescribed syllabus. The format is given since the question has not specified the method explicitly. Students can refer to the direct method for the knowledge purpose.