



# RELATE ACCOUNTS PRODUCTION



GUIDE TO

CASH FLOW STATEMENTS

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## SUPPORT SERVICES

Relate is committed to strong customer service and satisfaction. At all times you will be able to make contact with our company and technical services teams.

You can make contact with our support department in the following ways:

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### CUSTOMER SUPPORT

Relate Accounts Production has been built to reduce the amount of time users spent in checking and changing standard sets of accounts. We want users to be able to post in journals, make database adjustments and print a set of compliant accounts. Most of the time this is the case but there is one area which causes some users great difficulty.

That area is "Cash Flow Statements". Our support team offer as much support as possible in this area and if a user gets frustrated we will take the set of accounts, find the issue and send the information back to the user in order that they can produce the accounts.

Our support department deals with a wide variety of customers. We have everybody from the experienced formatters to juniors and admin staff who are unfamiliar with difficult areas of accounting such as loan movements and cash flow reconciliations. Often we are contacted by juniors who have no experience of cash flows and have been told to get the accounts finished and they are stuck. Often support faces users who are unable or unwilling to review their information and reconcile the cash flow in the right way.

To date we have taken cash flow queries and worked through the figures and sorted the cash flow on behalf of the accountant. Every single cash flow statement query we have received in 2014 has been down to incorrect postings by users in the accounts of their clients. As our user base grows Relate is unable to continue to have support staff tied up reconciling sets of accounts which the user should be able to do for themselves.

### IMPORTANT NOTICE

From the 1st December 2014 we will introduce a charge of €95 + VAT for any cash flow query we take in and we resolve through the normal explanation of incorrect postings. There will be a 3 day turnaround on cash flows from now on. This means we will endeavor to resolve your cash flow within 3 days or earlier. Our support staff does not know your clients' accounts or postings so you can appreciate it is difficult for them to jump into a set of your clients' accounts and resolved you're posting issues.

### HELP

In order to help users we have produced this detailed guide to cash flow statements which has 20 worked examples of the most common cash flow issues our support team has encountered. The majority of queries have been around the movements in comparatives. These are often the issue. In the next version of Relate Accounts Production we have introduced a validation check specifically for cash flow movements and this will also greatly help with reconciliations.

## CASH FLOW STATEMENT

### OVERVIEW

The Cash Flow Statement is prepared according to the standards laid down in International Accounting Standards - 7 (IAS -7) and in accordance with standard of Cash Flow FRS-102. The standard requires that cash flow be classified and shown in the Cash Flow Statements under three main headings, namely:

Cash generating from Operating Activities  
Cash generating from Investing Activities  
Cash generating from Financing Activities

There are two methods prescribed for the preparation of Cash Flow Statements and these are as follows:

Direct method of Cash Flow Statement  
Indirect method of Cash Flow statement

### COMPONENTS OF CASH FLOW STATEMENTS

#### **Operating Activities:**

Operating activities are the revenue producing activities of the enterprise that are not investing or financing activities.

#### **Investing Activities:**

Investing activities are the acquisition and disposal of assets and other investments. This activity includes transactions involving purchase and sale of assets like machinery, Land etc.

#### **Financing Activities:**

Financing activities are the activities that result in a change in the size and composition of owner's capital, preference share capital and borrowings of the enterprise.

### OPERATING ACTIVITIES

#### **Check List of preparation of Operating Cash Flow under Indirect Method:**

After computing the Net profit before tax and extraordinary items .i.e. operating profit, it is further adjusted the following items to arrive at net Cash Flow from Operating Activities. These adjustments are classified into two categories.

#### 1) Adjustments for Non-Cash Items:

Non – Cash items such as depreciation, interest on long term borrowing, discount on issue of shares or debenture written off, goodwill/ patent amortizations cost, amortization of government grants, loss on sale on assets or investments, premium payable on redemption of debentures or preferential shares etc are to be added back and non-operating incomes and gains such as profit on sale on fixed assets and investments, interest, rent or dividend received etc. are to be deducted.

## 2) Adjustments for changes in the current Assets and Current Liabilities:

A decrease in current assets and increase in current liabilities is added and an increase in current assets and a decrease in current liabilities are deducted from the operating profit.

Effect of Changes in current Assets and current Liabilities to be adjusted with operating profit as follows:

### **Current Assets**

#### *Accounts Receivable:*

Increases—subtract from net income to get operating cash flow

Decreases—add to net income to get operating cash flow

#### *Inventory:*

Increases—subtract from net income to get operating cash flow

Decreases—add to net income to get operating cash flow

#### *Other Current Assets (e.g., prepaid expenses):*

Increases—subtract from net income to get operating cash flow

Decreases—add to net income to get operating cash flow

### **Current Liabilities**

#### *Accounts and Trade Notes Payable:*

Increases—add to net income to get operating cash flow

Decreases—subtract from net income to get operating cash flow

#### *Other Liabilities (e.g., accruals), excluding nontrade payables:*

Increases—add to net income to get operating cash flow

Decreases—subtract from net income to get operating cash flow

EXAMPLE OF OPERATING CASH FLOW

Particulars	Current Year £	Previous Year £
<u>Cash Flow from Operating Activities</u>		
( A ) Net profit before Taxation and Extraordinary items	XXX	XXX
Adjustment for Non-cash and Non-operating items		
( B ) Add: Items to be added		
· Depreciation	XXX	XXX
· Preliminary expenses/Discount on issue of Shares & Debentures Written off	XXX	XXX
· Goodwill/patents/Trademarks Amortized	XXX	XXX
· Amortization of government grants	XXX	XXX
· Interest on borrowings & debentures	XXX	XXX
· Loss on sale of Fixed Assets	XXX	XXX
· Foreign Currency translations and transactions – Net	XXX	XXX
( C ) Less: Items to be deducted		
· Interest Income	XXX	XXX
· Dividend Income	XXX	XXX
· Rental Income	XXX	XXX
· Profit on sale of Fixed Assets	XXX	XXX
<u>Operating Profit before Working Capital changes (A+B-C)</u>	XXXX	XXXX

Particulars	Current Year £	Previous Year £
D ) <u>Operating Profit before Working Capital changes</u>	XXX	XXX
(E) Add: Decrease in Current Assets and Increase in Current Liabilities		
· Decrease in Stock/Inventories		
· Decrease in Debtors/Bills Receivables	XXX	XXX
· Decrease in Accrued Incomes	XXX	XXX
· Decrease in prepaid expenses	XXX	XXX
· Increase in creditors/Bills payables	XXX	XXX
· Increase in outstanding expenses	XXX	XXX
· Increase in Advance incomes	XXX	XXX
· Increase in Provision for Doubtful Debts    Decrease in Current Liabilities	XXX	XXX
	XXX	XXX
(F) Less: Increase in Current Assets and		
· Increase in Stocks/Inventories		
· Increase in Debtors/Bills Receivables		
· Increase in Accrued Incomes	XXX	XXX
· Increase in Prepaid expenses	XXX	XXX
· Decrease in creditors/Bills payables	XXX	XXX
· Decrease in outstanding expenses	XXX	XXX
· Decrease in Advance Incomes	XXX	XXX
· Decrease in Provision for Doubtful Debts	XXX	XXX
	XXX	XXX
(G) Cash Generated from Operations (D+E-F)	XXX	XXX
Less: Income Tax paid (Net of Tax Refund received)	XXXX	XXXX
Cash Flow before Extraordinary items    Extraordinary items (+/-)	XXX	XXX
Net cash from Operating Activities	XXXX	XXXX

## TAXATION

After that tax paid is to be deducted from cash generated from operations to arrive at the cash flow from operating activities before extraordinary items. After that we add or subtract the proceeds of extraordinary items to get Net Cash generated from operating activities.

We need to note that only tax paid during the year to be deducted from operating cash flow as the provision for tax represents the amount of tax provided for the current year. So it's added back to the current year's profit to calculate net profit before tax and extraordinary items. It is merely a book entry and does not involve outflow of cash and cash flow would not be affected if the provisions for tax entry pass in the accounts.



## ILLUSTRATION OF TAXATION ISSUE - NUMBER 1

XYZ Limited has made a tax provision during the current financial year amounting to £35 and the last year tax liability was £1,650. During the current year the company paid £1,620 out of a total tax liability of £1,685. So the company needs to post the following journal during the year as follows.

Code	Description	Type	Group	2013	
				Debit £	Credit £
501	Corporation tax current year	P/L	AdminCost	1,650.00	
831	Corporation tax payable	B/S	CurrCr		1,650.00
Code	Description	Type	Group	2014	
501	Corporation tax current year	P/L	Tax	35.00	
831	Corporation tax payable	B/S	CurrCr		35.00
<b>Payment Entry As Follows</b>					
832	Corporation tax paid	B/S	CurrCr	1,620.00	
771	Bank Current Account	B/S	BankCash		1,620.00

So in this case the tax paid during the year will reflect in the cash flow statement and the provision for taxation will be added back with the operating profit being the non cash transaction.

## ILLUSTRATION OF TAXATION ISSUE - NUMBER 2

XYX during the last financial year (i.e. year 2013) made a tax provision of £35 and has a total tax liability in that financial year of £75. On the basis of tax analysis it has come to knowledge that the company had needed to make provision for tax amount of £27.5 during the last financial year ( i.e. year 2013 ) and during the current financial year ( i.e. year 2014 ) company further made the provision of £37.5 and the tax paid during the year was £62.50. Following journals are required to be posted in this case.

Code	Description	Type	Group	2014	
				Debit £	Credit £
831	Corporation tax payable	B/S	CurrCr	7.50	
501.01	Corporation tax adjustment re: previous year	P/L	Tax		7.50
501	Corporation tax current year	P/L	Tax	37.50	
831	Corporation tax payable	B/S	CurrCr		37.50
<b>Payment Entry As Follows</b>					
832	Corporation tax paid	B/S	CurrCr	62.50	
771	Bank Current Account	B/S	BankCash		62.50

### ILLUSTRATION OF TAXATION ISSUE - NUMBER 3

Suppose XYZ had the tax liability of the last three years as £ 12500, £ 25000, £ 10000 i.e. for the year of 2014, 2013 and 2012 and the company had shown the tax liability under the nominal code 831 for such three year as £ 0, £ 26000, £ 10000. The company had paid the tax liability of those years as £ 12500, £ 26000, £ 9000. So the journal entries to be passed as under.

In the above case the cash flow statement will not be matched as the company had erroneously passed the tax liability of the current year as the tax liability of the current year had been shown as £ 0 instead of £ 12500. This is due to reason of as the company had set off the tax payment amount with the tax liability and as a result of the tax payment amount had not been reporting in the operating Cash Flow statement. So the company needs to pass the following journal entry in the current year.

Code	Description	Type	Group	2014	
				Debit £	Credit £
832	Corporation tax paid	B/S	CurrCr	12500	
831	Corporation tax payable	B/S	CurrCr		12500
832	Corporation tax paid	B/S	CurrCr	12500	
771	Bank Account	B/S	BankCash		12500

### ILLUSTRATION OF TAXATION ISSUE - NUMBER 4

On analysis of the tax liability of XYX Ltd during the current financial year (i.e. 2014) ,it has been observed that company was required to carry forward the balance of tax liability under the code 831 amounting of € 12501 but the company had carried forward opening balance of € 12500, so under mentioned rectification entry to be passed during the year.

Code	Description	Type	Group	2014	
				Debit £	Credit £
991	Profit and loss reserve retained profit b/fwd	B/S	RetPrBFwdMvt	1	
831	Corporation tax payable	B/S	CurrCr		1

## INVESTING ACTIVITIES

1. Investing activities of an enterprise are the acquisition and disposal of the assets and other investments.

Accordingly:

Cash inflow and outflow relating to the fixed assets

Shares and debt instruments of other enterprises

Interests in joint ventures

Advances and loans to third parties

Repayments

are all shown under investing activities in the cash flow statement.

2. Cash flow from investing activities is ascertained by analyzing the changes in fixed assets and long term investments in the beginning and at the end of the year.

### EXAMPLE OF INVESTING ACTIVITIES

Particulars	Current Year £	Previous Year £
Cash Flow from Investing Activities		
·Add: Proceeds from Sale of Fixed Assets	XXX	XXX
·Add: Proceeds from Sale of Investments	XXX	XXX
·Add: Proceeds from Sale of Intangible Assets	XXX	XXX
·Add: Interest and Dividend Received	XXX	XXX
·Add: Rent Income	XXX	XXX
·Less: Purchase of Fixed Asset	XXX	XXX
·Less: Purchase of Investment	XXX	XXX
·Less: Purchase of Intangible Assets like Goodwill	XXX	XXX
Net Cash from Investing Activities	XXXX	XXXX

**ILLUSTRATION OF OPERATING & INVESTING ACTIVITIES ISSUE - NUMBER 1**

XYZ.Co had purchased a motor vehicle 5 years ago with a price of £1,500 and the company charged the depreciation @ 10 % on the straight line method. The asset has a total life of 10 years with residual value of £100. As per the last annual accounts, the carried forward balance of the asset was £800 and the accumulated depreciation account was £700 and the company also purchased an additional motor vehicle amounting of £2,000 with a total life of the asset 10 years. The depreciation charged during the financial year amounted to £340. The following journal entry needs to be made during the year as follows.

Code	Description	Type	Group	2014	
				Debit £	Credit £
671.01	Motor Vehicle Addition Cost	B/S	TanFa	2,000.00	
813	Trade Creditors - posting account	B/S	CurrCr		2,000.00
813	Trade Creditors - posting account	B/S	CurrCr	2,000.00	
771	Bank Current Account	B/S	BankCash		2,000.00
397	Depreciation on Motor Vehicle	P/L	Tanfa	340.00	
672.01	Motor Vehicle Depreciation charge for the period	B/S	Tanfa		340.00

In the above case, the deprecation amount of £340 should be added back with net operating profit after tax, being non cash transaction and addition amount of new motor vehicle i.e. £2,000 would be treated as cash out flow from investing activities.

ILLUSTRATION OF OPERATING & INVESTING ACTIVITIES ISSUE - NUMBER 2

XYZ Ltd during the current financial year sold Furniture from their asset list at price of £2,700 and the asset was purchased 5 years ago at price of £5,200. The total accumulated depreciation charged up till last financial year was £1,976 and the depreciation charged for the current financial year was £494. So the under mentioned journal entries are needed in the accounts in the current financial year.

Code	Description	Type	Group	2014	
				Debit £	Credit £
771	Bank Current Account	B/S	BankCash	2,7000.00	
661.02	Fixtures, fittings and equipment cost of disposals	B/S	Tanfa		2,700.00
396	Depreciation on fixtures, fittings and equipment	P/L	AdminCost	494.00	
662.01	Fixtures, fittings and equipment depreciation charge for period	B/S	Tanfa		494.00
399.01	Profits/losses on disposal of intangibles	P/L	AdminCost	30.00	
662.02	Fixtures, fittings and equipment cost of disposals	B/S	Tanfa		30.00

In this case the accumulated depreciation of £1,976 in the last financial year would be carried forward under the code of 672 (i.e. Fixtures, fittings and equipment accumulated depreciation b/fwd) in the current financial year. Out flow of £2,700 would show as cash inflow from investing activities and the depreciation and loss on sale of furniture of £494 and £30 would be added back with operating profit being non cash transactions.

### ILLUSTRATION OF OPERATING & INVESTING ACTIVITIES ISSUE - NUMBER 3

XYZ .Co on the basis of their own verification, established that Furniture and Fixture having the WDV value of £, 2500 and has carrying value more than its recoverable amount and on the basis of testing of impairment, the company wants to make provision for diminution of said asset amounting to £125 and during the same year the company also charged the depreciation £250 as per the straight line method. So the under mentioned journal entries are needed in the accounts in the current financial year.

Code	Description	Type	Group	2014	
				Debit £	Credit £
366	Provision for diminution in value of fixed assets	P/L	AdminCost	125.00	
663.01	Fixtures, fittings and equipment cost impairment losses	B/S	Tanfa		125.00
396	Depreciation on fixtures, fittings and equipment	P/L	AdminCost	250.00	
662.01	Fixtures, fittings and equipment depreciation charge for period	B/S	Tanfa		250.00

In this case transaction showing provision for diminution in value of fixed assets and deprecation on fixtures, fittings and equipment would be added back with the operating profit since non cash transaction.

### ILLUSTRATION OF OPERATING & INVESTING ACTIVITIES ISSUE - NUMBER 4

XYZ. Co during the current year (i.e. 2014) signed an agreement with ABC .Co to acquire one of the multi brand products and according to the agreement; XYZ.Co can only sell the product in UK region. According to the brand valuation, XYZ.Co considered £ 12,500 as goodwill of that product. XYZ.Co wanted to write off the same goodwill over the terms of 5 years. So in this case accounting journal entries to be passed during there are as follows

Code	Description	Type	Group	2014	
				Debit £	Credit £
611.01	Goodwill additions	B/S	IntanFa	12,500.00	
813	Trade Creditors - posting account	B/S	CurrCr		12,500.00
813	Trade Creditors - posting account	B/S	CurrCr	12,500.00	
771	Bank current account	B/S	BankCash		12,500.00
391.03	Amortization of goodwill	P/L	AdminCost	2,500.00	
612.01	Goodwill depreciation charge for period	B/S	Intanfa		2,500.00

In this case the funds of £12,500 will be an outflow in the current financial year (i.e. 2014) would be treated as investing activity and in the goodwill depreciation charge of £2,500 would be added back to operating profit in the year 2014 being the non cash transaction.

#### ILLUSTRATION OF OPERATING & INVESTING ACTIVITIES ISSUE - NUMBER 5

ABC.Co acquired plant and machinery valued at £550 under the Hire purchase agreement and according to the agreement, the company would acquire the same asset over the period 8 years with the simple interest of 12 % p.a. During the current year the company paid interest £57 out of total EMI payment of £216. The Company also charged depreciation of @ 10 % on straight line method as the asset has total life of 10 years with the residual value of £50. So in this case accounting journal entries to be passed are as follows.

Code	Description	Type	Group	2014	
				Debit £	Credit £
651.01	Plant and machinery additions at cost	B/S	Tanfa	550.00	
813	Trade creditors - posting account	B/S	CurrCr		550.00
481	Hire purchase interest	P/L	IntPay	57.00	
921.01	Long term HP Liability increase	B/S	LtCred		57.00
813	Trade creditors - posting account	B/S	CurrCr	159.00	
921.02	Long term HP repayments	B/S	BankCash	57.00	
771	Bank current account 1	B/S	BankCash		216.00
395	Depreciation of plant and machinery	P/L	Admncost	50.00	
652.01	Plant and machinery depreciation charge for the period	B/S	Tanfa		50.00

In this case plant and machinery addition cost would be the cash outflow from investing activities and the depreciation charged on the asset and Hire purchase interest amount would be added back with the operating profit and the cash outflow from HP liability would be treated as financing activity .

The Financing Activities of an enterprise are those activities that result in change in the size and composition of owner's capital and borrowing of the enterprise. It includes proceeds such as:

- Issue of shares or other similar instruments
- Issue of debentures
- Loans
- Bonds
- other short-term loans or long term borrowings
- Repayments of amounts borrowed

accordingly, receipts and payments on account of the above are disclosed in the cash flow statement as the cash flow from financing activities

When shares are issued at a premium, the cash flow statement reflects the total cash generated by the issue (i.e., Face Value of shares + Premium). The cash flow from financing activities is ascertained by analyzing the change in Equity and Preference share capital, Debentures and other borrowings.



## EXAMPLE OF FINANCING ACTIVITIES

Particulars	Current Year £	Previous Year £
Cash Flow from Financing Activities		
· Add: Proceeds from issue of shares and Debentures	XXX	XXX
· Add: Proceeds from Other Long term Borrowings	XXX	XXX
· Less: Final Dividend Paid	XXX	XXX
· Less: Interim Dividend Paid	XXX	XXX
· Less: Interest on Debentures and Loans paid	XXX	XXX
· Less: Repayment of Loans	XXX	XXX
· Less: Redemption of Debentures/Preference shares	XXX	XXX
Net Cash from Financing Activities	XXXX	XXXX

## ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 1

Suppose X Ltd has borrowed a short term loan of £100 million @ 12 % on reducing interest rate from bank one year ago and current year B/Fwd loan balance £76.5 million and the company during the current year again borrowed £50 million. The company has the interest element of that loan amounting to £15.18 million and the company paid £15 million during the year and wants to transfer £25 million of a loan under long term payment. In such case cash generated from financing activities is as follows.

Code	Description	Type	Group	2014	2013
				£	£
807	Bank Loans short term b/fwd	B/S	CurrCr	76,500,000.00	
807.01	Bank Loans short increase	B/S	CurrCr	65,180,000.00	100,000,000.00
807.02	Bank Loans short term repayments	B/S	CurrCr	-15,000,000.00	-23,500,000.00
807.05	Bank Loans movement from long term	B/S	CurrCr	-25,000,000.00	
				<u>101,680,000.00</u>	<u>76,500,000.00</u>

The short term loan transfer to long term payment mode would have no effect in the cash flow statements as this only movement of loan amount from short term to long term accounts and amount would reflect in other charges segment in the notes of accounts of Analysis of changes in Net debt Account.

## ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 2

XYZ Ltd during the current financial year ( i.e. year 2014) has paid dividend of £1,250 to its share holders and such dividend was proposed by the board of director through the Annual General Meeting in last financial year ( i.e. 2013 ) Accounting entries would be passed in both of the years as follows.

Code	Description	Type	Group	2013	
				Debit	Credit
				£	£
881.02	Dividend accruals	B/S	CurrCr	1,250.00	
981.04	Capital contribution reserve other movement	B/S	OthRes		1,250.00
Code	Description	Type	Group	2014	
991	Retained Profit	B/S	RetPrBFwdMvt	1,250.00	
981	Capital contribution reserve b/fwd	B/S	OthRes		1,250.00
981.03	Capital contribution reserve dividend paid	B/S	OthRes	1,250.00	
771	Bank current account	B/S	BankCash		1,250.00

The proposed dividend for the last year becomes due and is also paid in current year. It is an outflow of cash and cash equivalents in the current year. So in this case proposed dividend of £ 1250 of last year would be added back with operating profit and the current year dividend paid amount would be the cash out flow from financing activities.

### ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 3

XX Ltd has brought forward credit card balance in current year from the last year amounting of £1,250.23 and during the current year the company paid £375.50 and the closing balance carried forward amounting to £874.73 and the company use code no 771.05 under the group of Current Creditor ( i.e. CurrCr ) to show all the credit card transactions.

In this case the cash flow statement would not be matched as the company showed all the transaction of credit card under the group of Current Creditor and credit card transaction needs to show under the group of Bank Cash (BankCash) so the company needs to use the code from 771 to 771.03 instead of 771.05.

### ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 4

Suppose XYZ ltd has created the special reserve account of £3,000 under the code of 987.01 in the last financial year (i.e. 2013) by debiting the code 381 (i.e. General Expenses A/C) and the company carried forward the special reserve balance current year (i.e. 2014) amounting of £3,000 under the code of 987. The Financing activities of the cash flow would not be matched due to the following reason.

In this case cash generated from the financing activities would not be matched in the last financial year as the special reserve account can be created only out of the profit of the company and same cannot be created by charging to expense account (i.e. general expense account in this case) and the movement of special reserve account needs to be shown under 987.03 (i.e. Special reserve movement to/from cash-based operating profit account). Following journal needs to be passed last year in order to rectify the cash flow statements.

Code	Description	Type	Group	2013	
				Debit £	Credit £
991.09	Profit and loss reserve other movement	B/S	RetPrBFwdMvt	3,000.00	
381	General Expenses	P/L	AdminCosts		3,000.00

## ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 5

Suppose XYZ Ltd during the last financial year generated the fund through the issue of preference Share capital amounting of £100,000.00 and the company used the code no 961.01 for the same and balance £100,000.00 carried forward during the current financial year under the code 961. In this case the cash flow statement would not be matched due to the following reason and same can be rectified as under.

Since fund raised from the issue of preference Share capital is a financial liability of the company so the company needs to use the code no 928.01 instead of code 961.01. To rectify the cash flow statement, the following journal needs to be passed.

Code	Description	Type	Group	2014	
				Debit £	Credit £
961.01	Preference equity share capital class 1 b/fwd	B/S	ShCap	100,000.00	
928.01	Shares classified as financial liabilities > 1 year b/fwd	B/S	LTCred		100,000.00

And the company needs to carry forward the balance of £100,000.00 under the code 928 during the current financial year.

## ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 6

XYZ has during the current year (i.e. 2014) carried forward balance of Ordinary equity share capital class 1 under the nominal code of 951 , amounting of £ 20,000.00 and such shares were issued to the share holders in the last financial year (i.e.) 2013 but in the last financial the company had shown the share capital amount under the nominal code of 951. So the under mentioned adjustment to be made in the comparative year (i.e.) in order to rectify the cash flow statement.

In this case the cash flow statement would not be matched as the increase in the share capital account had been shown under the nominal code 951 instead of 951.01. The rectification entry of the above illustration is as under

Code	Description	Type	Group	2013	
				Debit £	Credit £
951	Ordinary equity share capital class 1 b/fwd	B/S	ShCap	20,000.00	
951.01	Ordinary equity share capital class 1 cash issue	B/S	ShCap		20,000.00

### ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 7

XYZ has carried forward balance of Deferred Income government grants cost under the code of 944, from the financial year 2013 amounting of £800 and during the same year new fund received amounting of £3,500 under the code 944.01 but the company carried forward the balance during the financial year under the code 944 and 944.01 as £700 and £3,000 and the during the current financial year the company received £1,000 as towards the contribution of fund and same has been shown under the code of 944.01.

In this case the cash flow statement would have an error in financing activates amounting of £3,500 as the carried forward balance from the last year ( i.e. 2013) should be £4,300 and the new government grant received amount would be £1,000. So the following journal entries need to pass in order to rectify the cash flow statement.

Code	Description	Type	Group	2014	
				Debit	Credit
				£	£
944.01	Deferred income government grant increase	B/S	AccDefInc	3,500.00	
944	Deferred income government grant cost b/fwd	B/S	AccDefInc		3,500.00
777.01	Current Account	B/S	Bank Cash	1,000.00	
944.01	Deferred income government grant increase	B/S	AccDefInc		1,000.00

### ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 8

XYZ has carried forward the Long term HP balance and Long term HP repayment balance under the code no 921 and 921.02 as follows.

Code	Description	2014	2013	2012
		£	£	£
921	Long term HP liability balance b/fwd	0.00	-2,250.00	-6,350.00
921.01	Long term HP liability increase	0.00	2,250.00	0.00

In this case brought forward net fund would be differs from the comparative net debt -4099.50 and the same can be rectified in the following manner.

In the above case the company has carried forward the closing balance of long term HP Liability from the pre comparative year i.e. 2012 amounting of £2,250.50 under the code of 921 but the company did not show the Long term HP payment amount in the code no 921.01, So the following journal to be passed in the pre comparative year in order to rectify the cash flow statement.

Code	Description	Type	Group	2012	
				Debit	Credit
				£	£
921.01	Long term HP liability balance b/fwd	B/S	LTCred	4,099.50	
771or 782	Bank current Account or Cash control Account	B/S	BankCash		4,099.50

### ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 9

XYZ has total long term loan balance during the beginning of the current financial Year (i.e. 2014) amounting to £75,000 and out of which the company wants to transfer £15,000 to short term loan accounts and during the current year new short term loan raised amounting to £10,000. The journal entries to be passed in this case can be seen below.

Code	Description	Type	Group	2014	
				Debit £	Credit £
904.02	Long term bank loan movement to under 1 year	B/S	LTCred	15,000.00	
807.05	Bank loan movement from long term	B/S	LTCred		15,000.00
771	Bank Current Account	B/S	Bank Cash	10,000.00	
807.01	Bank loan short term increase	B/S	CurrCr		10,000.00

### ILLUSTRATION OF FINANCING ACTIVITIES ISSUE - NUMBER 10

Suppose YZX had the foreign exchange movement on debt of £ 25000 and the company had posted the same as a liability under the nominal code 910.04 and the company had the carried forward balance under the nominal code 910 of last year as £ 30000. During the current financial year ( i.e. ) the company had paid the £ 25000. So the company needs to pass the following journal and the rectification entries in the accounts.

Code	Description	Type	Group	2014	
				Debit £	Credit £
910.04	Foreign Exchange Movement on Debt	B/S	LTCred	25,000.00	
910.01	Foreign Exchange Movement on Debt	B/S	LTCred		25,000.00
910.02	Other long term loans movement to under 1 year	B/S	LTCred	25000.00	
807.05	Bank loan movement from long term	B/S	CurrCr		25000.00
<b>Payment</b>					
807.04	Bank Loan Short term repayment of long term	B/S	CurrCr	25000.00	
807.00	Bank loan short term b/fwd	B/S	CurrCr		25000.00

Note: Since the nominal code of 910.04 was reporting under 910.02 i.e. ( Other long term loans movement to under 1 year ), So the cash flow would not be matched and any increase in the other long term loan account would require to be shown under 910.01.

## CASH FLOW STATEMENT SUMMARY

Particulars	Current Year £	Previous Year £
Net cash inflow from operating activities	XXXX	XXXX
Taxation	XXXX	XXXX
Returns on investments and servicing of finance	XXXX	XXXX
Capital expenditure and financial investment	XXXX	XXXX
Less :		
Financing		
( A) Movement in cash in the year	XXXX	XXXX
Reconciliation of net cash flow to movement in net debt		
Movement in cash in the year ( A)	XXXX	XXXX
Cash inflow from increase in debts and lease financing	XXXX	XXXX
Change in net debt resulting from cash flow		
Net fund at the beginning of the year	XXXX	XXXX
	XXXX	XXXX
Net fund at the end of the year	XXXXX	XXXX

## SPECIAL ITEMS TREATED ON THE CASH FLOW STATEMENT

### INTERESTS AND DIVIDENDS

The treatment of interest and dividends received as well as paid depends on the nature of the business i.e., whether the business is of financial or non-financial nature. In case of a financial company, interest paid and dividend received is treated as an operating activities and the dividend paid would be financing activities and in case of other enterprises interest and dividend paid would be financing activities in nature.

### PROPOSED DIVIDENDS

The proposed dividend for the current year becomes due and is also paid in next year. It is an outflow of cash and cash equivalents in the next year.

The proposed dividend of the previous year becomes due and is also paid in the current year. It is an outflow of cash and cash equivalents in the current year

### ACCOUNTING TREATMENT OF THE PROPOSED DIVIDEND

- a) Proposed Dividend (current year): Add back to the current year's profits to find out cash from operating activities.  
 b) Proposed Dividend (Previous year): Net dividend paid (proposed dividend – dividend still payable) is cash used in financing

## COMPARATIVE ANALYSIS

Comparative analysis is one of main factor proving that whether the company is able to carry forward the debt properly from the last accounts and incase the comparative balances are not proper, the company needs to check the same from the cash flow statements proof and do the necessary rectifications entries to make sure that comparative balances are proper.

## ANALYSIS OF CHANGES IN NET DEBT

The company needs to reconcile the movement of cash in the period with the movement of debt as it would suggest whether the debt movement is proper with last year. In case the company wants to transfer any Short/ Long term debt to Long/Short term accounting code, such would be shown under the other charges section as this movement would not have any effect on cash flow statement. Following example shows how it needs to reconcile.

### EXAMPLE: ANALYSIS OF CHANGES IN NET DEBT NUMBER 1

Particulars	Opening Balance £	Cash Flow £	Other Charges £	Closing Balance £
Cash at bank and in hand	642,934	471,877	--	1,114,811
Overdrafts	(222,705)	(187,331)	--	(410,036)
	<u>420,229</u>	<u>284,546</u>	--	<u>704,775</u>
Debt due within one year	(91,281)	1,582	(232,969)	(322,668)
Debt due after one year	(138,043)	(712,299)	232,969	(617,373)
	<u>(229,324)</u>	<u>(710,717)</u>	--	<u>(940,041)</u>
Net debt	190,905	(426,171)	--	(940,041)



The cash statement proof is a major tool available in the software to analysis the movement of the cash and cash equivalent of the each activity.

There are two reconciliation statements available in the software in order to test the net fund to be carried forward for the comparative year as well as the current year and these are as under.

- a) **Reconciliation of net funds/debt in comparative to opening in current year**
- b) **Reconciliation of current net funds/debt to closing balance in analysis of changes to net funds/debt note**

Some of the points are to be tested and these are.

- 1) Movement of the operating activity
- 2) Movement of Debtors and Creditors cash Flow
- 3) Return on Investment and Servicing finance
- 4) Cash flow from taxation
- 5) Capital Expenditure investments
- 6) Cash flow from acquisition and disposal
- 7) Cash movement from the financing activities
- 8) Need to check the comparative and pre-comparative carried forward balances.

All the above movements to be reconciled with previous year net fund in order to compute the net fund to be carried for the next financial year and in case any irregularities are found in the movement of any of the above then there would be an error notes with the following descriptions for both the year.

- a) **The brought forward net funds/debt differs from the comparative net funds/debt by € XXX.**
- b) **The current net funds/debt differs from the closing balance in analysis of changes to net funds/debt note by € XXX**

The under mentioned illustrations will show the movement of cash and reconciliation statement of fund with that movement and the company needs to test this cash flow statement proof in order to rectify the cash flow statement.

**XYZ LTD***Cash Flow Statement Proof for the year ended 31 December 2013**Reconciliation of net funds/debt in comparative to opening in current year*

Cash Flow Heading Group	Description	2012	2011	for 2012
Operating surplus	Operating profit	6,600		6,600
	Creditors cash flow	900	-	
	Interest payable accrued	(10,500)	(620)	
Movement in creditors				(8,980)
Movement of debtors				--
<b>Net cash inflow from operating activities</b>				(2,380)
	Less: Interest receivable and payable accrued		620	
<b>Returns on investments and servicing of finance</b>				(620)
<b>Capital expenditure</b>	Cash flow capital expenditure and financial investment	(47,877)		(47,877)
				(50,877)
	Cash flow finance (excluding change in hire purchase interest prepaid)	60,980		
<b>Finance</b>				60,980
<b>Movement in cash</b>				10,103
	Cash flow finance (excluding change in hire purchase interest prepaid)	(60,980)		
Cash inflow from increase in debts and lease financing				(60,980)
Change in net debt resulting from cash flows				(50,877)
	Cash flow net debt b/fwd	(131,150)		
	Less: Cash flow bank		(4,398)	
<b>Net debt at 1 January 2012</b>				(126,752)
<b>Net debt at 31 December 2012</b>				(177,629)
				<b>B/Fwd net funds</b>
<b>Cash Flow Note Heading</b>	<b>Group Description</b>	<b>2013</b>	<b>2012</b>	<b>for 2013</b>
Cash at bank and in hand	Bank and cash		15,540	15,540
Debt due after one year	Cash flow long term debt b/fwd	(193,169)		(193,169)
<b>Net funds at 31 December 2012</b>				(177,629)

**XYZ LTD***Cash Flow Statement Proof for the year ended 31 December 2013***Reconciliation of current net funds/debt to closing balance in analysis of changes to net funds/debt note**

<b>Cash Flow Heading Group</b>	<b>Description</b>	<b>2013</b>	<b>2012</b>	<b>Cash Flow for 2013</b>
Operating surplus	Operating profit	75,000		75,000
Depreciation				962
Creditors cash flow		1,707	900	
Interest payable accrued		(9,067)	(10,461)	
Movement in creditors				2,201
Movement of debtors				---
<b>Net cash inflow from operating activities</b>				<u>78,163</u>
	Less: Interest receivable and payable accrued		10,461	
<b>Returns on investments and servicing of finance</b>				<u>(10,461)</u>
<b>Capital expenditure</b>	Cash flow capital expenditure and financial investment	(18,155)		(18,155)
				<u>49,547</u>
	Cash flow finance (excluding change in hire purchase interest prepaid)	(60,000)		
<b>Finance</b>				<u>(60,000)</u>
<b>Movement in cash</b>				<u>(10,453)</u>
	Cash flow finance (excluding change in hire purchase interest prepaid)	(60,000)		
Cash inflow from increase in debts and lease financing				<u>60,000</u>
Change in net debt resulting from cash flows				<u>49,547</u>
	Cash flow net debt b/fwd	(193,169)		
	Less: Cash flow bank		(15,540)	
<b>Net debt at 1 January 2013</b>				<u>(177,629)</u>
<b>Net debt at 31 December 2013</b>				<u><u>(128,082)</u></u>
<b>Cash Flow Note Heading</b>	<b>Group Description</b>	<b>2013</b>	<b>2012</b>	<b>Closing net funds for 2013</b>
Opening balance at 1 January 2013				(177,629)
Cash at bank and in hand	Bank and cash	5,087	15,540	(10,453)
				<u>(187,341)</u>
Debt due after one year	Cash flow debt over 1 yr	60,000		60,000
<b>Net funds at 31 December 2013</b>				<u><u>(128,082)</u></u>

**NOTE:**If you have anything you would like added or included in this guide please email [info@relate-software.com](mailto:info@relate-software.com).