Exposure Draft

Accounting Standard (AS) 7

Statement of Cash Flows

Last date for the comments: January 21, 2016

Issued by

Accounting Standards Board

The Institute of Chartered Accountants of India

Exposure Draft

Accounting Standard (AS) 7, Statement of Cash Flows

(The Indian Accounting Standards (Ind AS), as notified by the Ministry of Corporate Affairs in February, 2015, have been applicable to the specified class of companies. For other class of companies, i.e., primarily the unlisted entities having net worth less than Rs. 250 crores, Accounting Standards, as notified under Companies (Accounting Standards) Rules, 2006, has been applicable. However, the Ministry of Corporate Affairs has requested the Accounting Standards Board of The Institute of Chartered Accountants of India (ICAI) to update Accounting Standards, as notified under Companies (Accounting Standards) Rules, 2006, to bring them nearer to Indian Accounting Standards. Accordingly, the Accounting Standards Board, ICAI, initiated to update these standards which will be applicable to all companies having net-worth less than Rs. 250 crores including non-corporate entities. While formulating these Accounting Standards, the Accounting Standards Board, ICAI, decided to maintain the consistency with the paragraph numbers and with the numbering of Standards of the Indian Accounting Standards.)

In this direction, following is the Exposure Draft of the updated Accounting Standard (AS) 7, Statement of Cash Flows, issued by the Accounting Standards Board of the ICAI, for comments. The Board invites comments on any aspect of this Exposure Draft, particularly on the questions set out below. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

Question for respondents
In order to avoid complexity for smaller entities, the Board proposes to amend paragraph 14 of this standard by deleting the requirement of classifying the cash payments to manufacture or acquire assets held for rental to others and subsequently held for sale and cash receipts from rents and subsequent sales of such assets as cash flows from operating activities. This requirement is deleted because it was felt that the application of the same would be too onerous for entities not applying Ind ASs. The said requirement is also proposed to be deleted from updated AS 16, *Property, Plant and Equipments.* Do you agree with the proposed amendments? If not, why and what alternative do you propose?

Comments can be submitted using one of the following methods so as to receive not later than January 21, 2016:

1.	*Electronically:*	*click on* ***http://www.icai.org/comments/asb/*** *to submit comments online*
2.	*Email:*	*Comments can be sent at commentsasb@icai.in*
3.	*Postal:*	*Secretary, Accounting Standards Board,* *The Institute of Chartered Accountants of India,* *ICAI Bhawan, Post Box No. 7100,* *Indraprastha Marg, New Delhi – 110 002*

Further clarifications on any aspect of this Exposure Draft may be sought by e-mail to nikita.bothra@icai.in

Accounting Standard (AS) 7
Statement of Cash Flows

*(This Accounting Standard includes paragraphs set in **bold** type and plain type, which have equal authority. Paragraphs in **bold** type indicate the main principles.)*

Objective

Information about the cash flows of an entity is useful in providing users of financial statements with a basis to assess the ability of the entity to generate cash and cash equivalents and the needs of the entity to utilise those cash flows. The economic decisions that are taken by users require an evaluation of the ability of an entity to generate cash and cash equivalents and the timing and certainty of their generation.

The objective of this Standard is to require the provision of information about the historical changes in cash and cash equivalents of an entity by means of a statement of cash flows which classifies cash flows during the period from operating, investing and financing activities.

Scope

1 An entity shall prepare a statement of cash flows in accordance with the requirements of this Standard and shall present it as an integral part of its financial statements for each period for which financial statements are presented.

2 [Refer Appendix 1]

3 [Refer Appendix 1]

4 [Refer Appendix 1]

5 [Refer Appendix 1]

Definitions

6 The following terms are used in this Standard with the meanings specified:

6.1 ***Cash*** **comprises cash on hand and demand deposits.**

6.2 ***Cash equivalents*** **are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.**

6.3 ***Cash flows*** **are inflows and outflows of cash and cash equivalents.**

6.4 ***Operating activities*** **are the principal revenue-producing activities of the entity and other activities that are not investing or financing activities.**

6.5 ***Investing activities*** **are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.**

6.6 ***Financing activities*** **are activities that result in changes in the size and composition of the contributed equity and borrowings of the entity.**

Cash and cash equivalents

7 Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. For an investment to qualify as a cash equivalent it must be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. Equity investments are excluded from cash equivalents unless they are, in substance, cash equivalents, for example in the case of preference shares acquired within a short period of their maturity and with a specified redemption date.

8 Bank borrowings are generally considered to be financing activities. However, in some cases, bank overdrafts which are repayable on demand form an integral part of an entity's cash management. In such cases, bank overdrafts are included as a component of cash and cash equivalents. A characteristic of such banking arrangements is that the bank balance often fluctuates from being positive to overdrawn.

9 Cash flows exclude movements between items that constitute cash or cash equivalents because these components are part of the cash management of an entity rather than part of its operating, investing and financing activities. Cash management includes the investment of excess cash in cash equivalents.

Presentation of a statement of cash flows

10 The statement of cash flows shall report cash flows during the period classified by operating, investing and financing activities.

11 An entity presents its cash flows from operating, investing and financing activities in a manner which is most appropriate to its business. Classification by activity provides information that allows users to assess the impact of those activities on the financial position of the entity and the amount of its cash and cash equivalents. This information may also be used to evaluate the relationships among those activities.

12 A single transaction may include cash flows that are classified differently. For example, when the installment paid in respect of an item of Property, Plant and Equipment

acquired on deferred payment basis includes interest, the interest element is classified under financing activities and the loan element is classified under investing activities.

Operating activities

13 The amount of cash flows arising from operating activities is a key indicator of the extent to which the operations of the entity have generated sufficient cash flows to repay loans, maintain the operating capability of the entity, pay dividends and make new investments without recourse to external sources of financing. Information about the specific components of historical operating cash flows is useful, in conjunction with other information, in forecasting future operating cash flows.

14 Cash flows from operating activities are primarily derived from the principal revenue-producing activities of the entity. Therefore, they generally result from the transactions and other events that enter into the determination of profit or loss. 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;

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

(f) 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 that is included in recognised profit or loss. The cash flows relating to such transactions are cash flows from investing activities.

15 An entity may hold securities and loans for dealing or trading purposes, in which case they are similar to inventory acquired specifically for resale. Therefore, cash flows arising from the purchase and sale of dealing or trading securities are classified as operating activities. Similarly, cash advances and loans made by financial institutions are usually classified as operating activities since they relate to the main revenue-producing activity of that entity.

Investing activities

16 The separate disclosure of cash flows arising from investing activities is important because the cash flows represent the extent to which expenditures have been made for

resources intended to generate future income and cash flows. Only expenditures that result in a recognized asset in the balance sheet are eligible for classification as investing activities. Examples of cash flows arising from investing activities are:

(a) cash payments to acquire property, plant and equipment, intangibles and other long-term assets. These payments include those relating to capitalised development costs and self-constructed property, plant and equipment;

(b) cash receipts from sales of property, plant and equipment, intangibles and other long-term assets;

(c) cash payments to acquire equity or debt instruments of other entities and interests in joint ventures (other than payments for those instruments considered to be cash equivalents or those held for dealing or trading purposes);

(d) cash receipts from sales of equity or debt instruments of other entities and interests in joint ventures (other than receipts for those instruments considered to be cash equivalents and those held for dealing or trading purposes);

(e) cash advances and loans made to other parties (other than advances and loans made by a financial institution);

(f) cash receipts from the repayment of advances and loans made to other parties (other than advances and loans of a financial institution);

(g) cash payments for futures contracts, forward contracts, option contracts and swap contracts except when the contracts are held for dealing or trading purposes, or the payments are classified as financing activities; and

(h) cash receipts from futures contracts, forward contracts, option contracts and swap contracts except when the contracts are held for dealing or trading purposes, or the receipts are classified as financing activities.

When a contract is accounted for as a hedge of an identifiable position, the cash flows of the contract are classified in the same manner as the cash flows of the position being hedged.

Financing activities

17 The separate disclosure of cash flows arising from financing activities is important because it is useful in predicting claims on future cash flows by providers of capital to the entity. Examples of cash flows arising from financing activities are:

(a) cash proceeds from issuing shares or other equity instruments;

(b) cash payments to owners to acquire or redeem the entity's shares;

(c) cash proceeds from issuing debentures, loans, notes, bonds, mortgages and other short-term or long-term borrowings;

(d) cash repayments of amounts borrowed; and

(e) cash payments by a lessee for the reduction of the outstanding liability relating to a finance lease.

Reporting cash flows from operating activities

18 An entity shall report cash flows from operating activities using either:

(a) the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed; or

(b) the indirect method, whereby profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows.

19 Entities are encouraged to report cash flows from operating activities using the direct method. The direct method provides information which may be useful in estimating future cash flows and which is not available under the indirect method. Under the direct method, information about major classes of gross cash receipts and gross cash payments may be obtained either:

(a) from the accounting records of the entity; or

(b) by adjusting sales, cost of sales (interest and similar income and interest expense and similar charges for a financial institution) and other items in the statement of profit and loss for:

(i) changes during the period in inventories and operating receivables and payables;

(ii) other non-cash items; and

(iii) other items for which the cash effects are investing or financing cash flows.

20 Under the indirect method, the net cash flow from operating activities is determined by adjusting profit or loss for the effects of:

(a) changes during the period in inventories and operating receivables and payables;

(b) non-cash items such as depreciation, provisions, deferred taxes, unrealised foreign currency gains and losses, and undistributed profits of associates; and

(c) all other items for which the cash effects are investing or financing cash flows.

Alternatively, the net cash flow from operating activities may be presented under the indirect method by showing the revenues and expenses disclosed in the statement of profit and loss and the changes during the period in inventories and operating receivables and payables.

Reporting cash flows from investing and financing activities

21 An entity shall report separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities, except to the extent that cash flows described in paragraphs 22 and 24 are reported on a net basis.

Reporting cash flows on a net basis

22 Cash flows arising from the following operating, investing or financing activities may be reported on a net basis:

(a) cash receipts and payments on behalf of customers when the cash flows reflect the activities of the customer rather than those of the entity; and

(b) cash receipts and payments for items in which the turnover is quick, the amounts are large, and the maturities are short.

23 Examples of cash receipts and payments referred to in paragraph 22(a) are:

(a) the acceptance and repayment of demand deposits of a bank;

(b) funds held for customers by an investment entity; and

(c) rents collected on behalf of, and paid over to, the owners of properties.

23A Examples of cash receipts and payments referred to in paragraph 22(b) are advances made for, and the repayment of:

(a) principal amounts relating to credit card customers;

(b) the purchase and sale of investments; and

(c) other short-term borrowings, for example, those which have a maturity period of three months or less.

24 Cash flows arising from each of the following activities of a financial institution may be reported on a net basis:

(a) cash receipts and payments for the acceptance and repayment of deposits

with a fixed maturity date;

(b) the placement of deposits with and withdrawal of deposits from other financial institutions; and

(c) cash advances and loans made to customers and the repayment of those advances and loans.

Foreign currency cash flows

25 Cash flows arising from transactions in a foreign currency shall be recorded in an entity's presentation currency by applying to the foreign currency amount the exchange rate between the presentation currency and the foreign currency at the date of the cash flow.

26 The cash flows of a foreign subsidiary shall be translated at the exchange rates between the presentation currency of the parent and the foreign currency at the dates of the cash flows.

27 Cash flows denominated in a foreign currency are reported in a manner consistent with AS 21, *The Effects of Changes in Foreign Exchange Rates.* This permits the use of an exchange rate that approximates the actual rate. However, AS 21 does not permit use of the exchange rate at the end of the reporting period when translating the cash flows of a foreign subsidiary.

28 Unrealised gains and losses arising from changes in foreign currency exchange rates are not cash flows. However, the effect of exchange rate changes on cash and cash equivalents held or due in a foreign currency is reported in the statement of cash flows in order to reconcile cash and cash equivalents at the beginning and the end of the period. This amount is presented separately from cash flows from operating, investing and financing activities and includes the differences, if any, had those cash flows been reported at end of period exchange rates.

29 [Refer Appendix 1]

30 [Refer Appendix 1]

Interest and dividends

31 Cash flows from interest and dividends received and paid shall each be disclosed separately. Cash flows arising from interest paid and interest and dividends received in the case of a financial institution shall be classified as cash flows arising from operating activities. In the case of other entities, cash flows arising from interest paid shall be classified as cash flows from financing activities while interest and dividends received shall be classified as cash flows from investing activities. Dividends paid shall be classified as cash flows from financing activities.

32 The total amount of interest paid during a period is disclosed in the statement of cash flows whether it has been recognised as an expense in profit or loss or capitalised in accordance with AS 23, *Borrowing Costs*.

33 Interest paid and interest and dividends received are usually classified as operating cash flows for a financial institution. However, there is no consensus on the classification of these cash flows for other entities. Some argue that interest paid and interest and dividends received may be classified as operating cash flows because they enter into the determination of profit or loss. However, it is more appropriate that interest paid and interest and dividends received are classified as financing cash flows and investing cash flows respectively, because they are costs of obtaining financial resources or returns on investments.

34 Some argue that dividends paid may be classified as a component of cash flows from operating activities in order to assist users to determine the ability of an entity to pay dividends out of operating cash flows. However, it is considered more appropriate that dividends paid shall be classified as cash flows from financing activities because they are cost of obtaining financial resources.

Taxes on income

35 Cash flows arising from taxes on income shall be separately disclosed and shall be classified as cash flows from operating activities unless they can be specifically identified with financing and investing activities.

36 Taxes on income arise on transactions that give rise to cash flows that are classified as operating, investing or financing activities in a statement of cash flows. While tax expense may be readily identifiable with investing or financing activities, the related tax cash flows are often impracticable to identify and may arise in a different period from the cash flows of the underlying transaction. Therefore, taxes paid are usually classified as cash flows from operating activities. However, when it is practicable to identify the tax cash flow with an individual transaction that gives rise to cash flows that are classified as investing or financing activities the tax cash flow is classified as an investing or financing activity as appropriate. When tax cash flows are allocated over more than one class of activity, the total amount of taxes paid is disclosed.

Investments in subsidiaries, associates and joint ventures

37 When accounting for an investment in an associate, a joint venture or a subsidiary accounted for by use of the equity or cost method, an investor restricts its reporting in the statement of cash flows to the cash flows between itself and the investee, for example, to dividends and advances.

38 An entity that reports its interest in an associate or a joint venture using the equity method includes in its statement of cash flows the cash flows in respect of its investments

in the associate or joint venture, and distributions and other payments or receipts between it and the associate or joint venture.

Changes in ownership interests in subsidiaries and other businesses

39 The aggregate cash flows arising from obtaining or losing control of subsidiaries or other businesses shall be presented separately and classified as investing activities.

40 An entity shall disclose, in aggregate, in respect of both obtaining and losing control of subsidiaries or other businesses during the period each of the following:

(a) the total consideration paid or received; and

(b) the portion of the consideration consisting of cash and cash equivalents.

(c) [Refer Appendix 1]

(d) [Refer Appendix 1]

40A [Refer Appendix 1]

41 [Refer Appendix 1]

42 [Refer Appendix 1]

42A Cash flows arising from changes in ownership interests in a subsidiary that do not result in a loss of control shall be classified as cash flows from financing activities , unless the subsidiary is held by an investment entity, as defined in AS 110, and is required to be measured at fair value through profit or loss.

42B [Refer Appendix 1]

Non-cash transactions

43 Investing and financing transactions that do not require the use of cash or cash equivalents shall be excluded from a statement of cash flows. Such transactions shall be disclosed elsewhere in the financial statements in a way that provides all the relevant information about these investing and financing activities.

44 Many investing and financing activities do not have a direct impact on current cash flows although they do affect the capital and asset structure of an entity. The exclusion of non-cash transactions from the statement of cash flows is consistent with the objective of a statement of cash flows as these items do not involve cash flows in the current period. Examples of non-cash transactions are:

(a) the acquisition of assets either by assuming directly related liabilities or by means

of a finance lease;

(b) the acquisition of an entity by means of an equity issue; and

(c) the conversion of debt to equity.

Components of cash and cash equivalents

45 An entity shall disclose the components of cash and cash equivalents and shall present a reconciliation of the amounts in its statement of cash flows with the equivalent items reported in the balance sheet.

46 In view of the variety of cash management practices and banking arrangements around the world and in order to comply with AS 1, *Presentation of Financial Statements*, an entity discloses the policy which it adopts in determining the composition of cash and cash equivalents.

47 The effect of any change in the policy for determining components of cash and cash equivalents is reported in accordance with AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*.

Other disclosures

48 An entity shall disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the entity that are not available for use by the group[1].

49 There are various circumstances in which cash and cash equivalent balances held by an entity are not available for use by the group[2]. Examples include cash and cash equivalent balances held by a subsidiary that operates in a country where exchange controls or other legal restrictions apply when the balances are not available for general use by the parent or other subsidiaries.

50 Additional information may be relevant to users in understanding the financial position and liquidity of an entity. Disclosure of this information, together with a commentary by management, is encouraged and may include:

(a) the amount of undrawn borrowing facilities that may be available for future operating activities and to settle capital commitments, indicating any restrictions on the use of these facilities;

(b) [Refer Appendix 1]

[1]The requirements shall be equally applicable to the entities in case of separate financial statements also.

[2]Ibid.

(c) the aggregate amount of cash flows that represent increases in operating capacity separately from those cash flows that are required to maintain operating capacity; and

(d) [Refer Appendix 1]

51 [Refer Appendix 1]

52 [Refer Appendix 1]

Appendix 1

Note: This Appendix is not a part of the Accounting Standard. The purpose of this Appendix is only to bring out the major differences, if any, between Accounting Standard (AS) 7 and the corresponding Indian Accounting Standard (Ind AS) 7, Statement of Cash Flows.

Comparison with Ind AS 7, *Statement of Cash Flows*

AS 7 differs from Indian Accounting Standard (Ind AS) 7, *Statement of Cash Flows*, in the following major respects:

1. Ind AS 7 contains paragraphs 3, 4 and 5 that explain the benefits of cash flow information. The said paragraphs and related heading are deleted in AS 7.

2. Ind AS 7 uses the term functional currency pursuant to the requirement of Ind AS 11. In AS the concept of functional currency is not there. As a consequence the term presentation currency is used wherever applicable.

3. Paragraph 14 of AS 7 is amended by deleting the requirement of classifying the cash payments to manufacture or acquire assets held for rental to others and subsequently held for sale and cash receipts from rents and subsequent sales of such assets as cash flows from operating activities. The said requirement is deleted, since; the same is based on the concept of substance over form pertaining to the business model of the entity which would be too cumbersome for smaller entities. The relevant requirement is stated in paragraph 68A of Ind AS 16, *Property, Plant and Equipments.*

4. AS 7 has reduced disclosure requirements as these are applicable to smaller entities, consequently following paragraphs are deleted in AS 7, however, in order to maintain consistency with paragraph numbers of Ind AS 7, the paragraph numbers are retained:
   (i) Paragraphs 40(c) and (d)
   (ii) Paragraphs 40A to 42
   (iii) Paragraph 42B
   (iv) Paragraph 50(d)
   (v) Paragraphs 51-52

5. The following paragraph numbers are deleted in Ind AS 7. In order to maintain consistency with paragraph numbers of Ind AS 7, the paragraph numbers are retained in AS 7:
   (i) paragraph 2
   (ii) paragraph 29
   (iii) paragraph 30
   (iv) paragraph 50(b)