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## *Trainee Accountant Webinar*

# ***F2 – Financial Accounting Presented By: Sandra Gleeson***

## Introduction

- The purpose of this webinar is to give an overview of the topic of the Statement of Cash Flows as examinable in F2 Financial Accounting.
- This webinar will focus on how to calculate cash flows using T-accounts and other reconciling workings and will also focus on the presentation of the cash flows in the proforma layout for a Statement of Cash Flows.

*Note – The examples used are taken from Question 5 of the April 2017 Formation 2 Financial Accounting exam paper*

## Why prepare a statement of cash flows?

- One of the statements which form part of the primary financial statements.
  - **Statement of Comprehensive Income.**
  - **Statement of Financial Position**
  - **Statement of Cash Flows**
- Each statement provides different information needed by users of financial statements

# Layout of the Statement of Cash Flows

Heading	Note
<b>Operating Activities</b>	These are the main revenue-producing activities of the entity that are not investing or financing activities, i.e. cash received from customers and cash paid to suppliers and employees.
<b>Investing Activities</b>	These are the acquisition and disposal of long-term assets and other investments (other than cash equivalents) i.e. cash paid to acquire fixed assets, cash received from disposal of fixed assets.
<b>Financing Activities</b>	These are the activities that alter the equity capital and borrowing structure of the entity i.e. cash received from issue of shares or debentures, cash paid for redemption of loans.
<b>= Increase or decrease in cash &amp; cash equivalents</b>	This figure should reconcile to the net difference in cash and cash equivalents as per the balance sheet at the current accounting period to the balance sheet at the end of the previous accounting period.

## Operating Activities – Direct Method

- The **direct method** shows each major class of gross cash receipts and gross cash payments.

Operating Activities	€
Cash receipts from customers	X
Cash paid to suppliers	(X)
Cash paid to employees	(X)
Cash paid for other operating expenses	(X)
Interest paid	(X)
Income taxes paid	<u>(X)</u>
<b>Net cash from operating activities</b>	<b><u>X</u></b>

## Operating Activities – Indirect Method

- The **indirect method** adjusts the accrual basis net profit or loss for the effects of non-cash transactions.

Operating Activities		€
Profit before tax		X
Add back depreciation & loss on disposal of assets (deduct profit on disposal)		X
Add back interest expense		X
Increase or Decrease in receivables		(X) / X
Increase or Decrease in inventories		(X) / X
Increase or Decrease in trade payables		X / (X)
Interest paid		(X)
Income taxes paid		<u>(X)</u>
<b>Net cash from operating activities</b>		<b><u>X</u></b>

## Investing Activities

- Any cash paid or received in relation to investment in long-term assets should be presented here.

Investing Activities	€	€
Cash received from disposal of assets	X	
Cash paid for acquisition of assets	(X)	
Interest received (could instead be shown in operating activities)	X	
Dividends received (could instead be shown in operating activities)	X	
<b>Net cash from investing activities</b>		<b><u>X/(X)</u></b>

## Financing Activities

- Any cash paid or received in relation to equity and debt should be presented here.

Financing Activities	€	€
Cash received from issue of equity	X	
Cash received from borrowings	X	
Cash paid for repayment of borrowings (including finance leases)	(X)	
Dividends paid (could instead be shown in operating activities)	X	
<b>Net cash from financing activities</b>		<b><u>X/(X)</u></b>

## Q5 April 2017 – Total Assets

### Falylk Ltd Statement of Financial Position as at 31 December 2016

	2016 €'000	2015 €'000
<b>Non-Current Assets</b>		
Property, Plant & Equipment (PPE)	5,120	3,940
<b>Total Non-Current Assets</b>	<b><u>5,120</u></b>	<b><u>3,940</u></b>
<b>Current Assets</b>		
Inventories	1,380	1,220
Trade Receivables	780	680
Cash & Cash Equivalents	50	112
<b>Total Current Assets</b>	<b><u>2,210</u></b>	<b><u>2,012</u></b>
<b>Total Assets</b>	<b><u>7,330</u></b>	<b><u>5,952</u></b>

## Q5 April 2017 - Equity

<b>Equity &amp; Liabilities</b>	=====	=====
Equity		
Share Capital	240	200
Share Premium	60	50
Retained Earnings	3,798	2,402
Revaluation Surplus	120	80
<b>Total Equity</b>	<b><u>4,218</u></b>	<b><u>2,732</u></b>

## Q5 April 2017 – Total Liabilities

<b>Non-Current Liabilities</b>	=====	=====
Long Term Loan	1,500	1,600
<b>Total Non-Current Liabilities</b>	<b><u>1,500</u></b>	<b><u>1,600</u></b>
<b>Current Liabilities</b>	=====	=====
Trade Payables	1,470	1,500
Bank Overdraft	32	60
Current Tax Payables	110	60
<b>Total Current Liabilities</b>	<b><u>1,612</u></b>	<b><u>1,620</u></b>

## Q5 April 2017 – Notes

### Notes:

- (i) The company's profit for the year before tax amounted to €1,476,000.
- (ii) The company's income tax expense for the year was €80,000.
- (iii) The cost of Property, Plant & Equipment (PPE) at 1 January 2016 amounted to €4,860,000. The company's depreciation policy is to depreciate all assets at 20% straight line on cost from the date of purchase to the date of sale. The additions to PPE occurred on 31 December 2016. On 1 July 2016, the company sold PPE which originally had cost €1,000,000. On the date this PPE was sold, its carrying value was €600,000 and the firm made a loss on the sale of the PPE of €40,000. The revaluation was performed on 31 December 2016.
- (iv) The company's finance cost for the year equals its cash payment of €92,000.

## Operating Activities – April 2016 Q5

Let's start by inserting the information readily available in the question

Operating Activities		€
Profit before tax (given in note (i))		1,476,000
Add back depreciation		(working required)
Add back loss on disposal (given in note (iii))		40,000
Add back interest expense (given in note (iv))		92,000
Increase or Decrease in receivables		(working required)
Increase or Decrease in inventories		(working required)
Increase or Decrease in trade payables		(working required)
Interest paid (given in note (iv))		(92,000)
Income taxes paid		(working required)
<b>Net cash from operating activities</b>		<b><u>X</u></b>

## Operating Activities – April 2016 Q5

### Calculation of depreciation

The company's depreciation policy is to depreciate all assets at 20% straight line on cost from the date of purchase to the date of sale.

	€
Cost of assets held for the full year (B/f 4,860,000 – Disposals 1,000,000) x 20%	772,000
Disposal 1 July (1,000,000 x 20% x 6/12)	100,000
Acquisition 31 December – (no depreciation for one day)	<u>0</u>
Depreciation charge for year	<u>872,000</u>

## Operating Activities – April 2016 Q5

Insert the depreciation amount

Operating Activities		€
Profit before tax (given in note (i))		1,476,000
<b>Add back depreciation</b>		<b>872,000</b>
Add back loss on disposal (given in note (iii))		40,000
Add back interest expense (given in note (iv))		92,000
Increase or Decrease in receivables		(working required)
Increase or Decrease in inventories		(working required)
Increase or Decrease in trade payables		(working required)
Interest paid (given in note (iv))		(92,000)
Income taxes paid		(working required)
<b>Net cash from operating activities</b>		<b>X</b>



## Operating Activities – April 2016 Q5

### Calculation of increases/decreases in working capital

- This is done by comparing the balance from the statement of financial position from 2015 to 2016

	2016	2015	Increase/Decrease
Inventories	1,380,000	1,220,000	Increase 160,000
Trade Receivables	780,000	680,000	Increase 100,000
Trade Payables	1,470,000	1,500,000	Decrease 30,000

## Operating Activities – April 2016 Q5

### How to remember what to do with increases and decreases in working capital

- Receivables – an increase in credit given to customers means less cash is received
- Inventory – an increase in inventory means goods were purchased which were not sold, so less cash received
- Payables – an increase in payables means creditors were paid sooner and more cash is spent

## Operating Activities – April 2016 Q5

### How to remember what to do with increases and decreases in working capital

Illustration of receivables using a T-Account

Receivables			
Balance b/f	100,000	Bank	540,000
Sales	<u>560,000</u>	Balance c/f	<u>120,000</u>
	<u>660,000</u>		<u>660,000</u>

The increase in receivables is €20,000. Note also that this is the same as the difference between Sales and Bank.

## Operating Activities – April 2016 Q5

### How to remember what to do with increases and decreases in working capital

	Increase	Decrease
Inventories	Deduct	Add
Trade Receivables	Deduct	Add
Trade Payables	Add	Deduct

## Operating Activities – April 2016 Q5

Insert working capital movement

Operating Activities		€
Profit before tax (given in note (i))		1,476,000
Add back depreciation		872,000
Add back loss on disposal (given in note (iii))		40,000
Add back interest expense (given in note (iv))		92,000
Increase in receivables		(160,000)
Increase in inventories		(100,000)
Decrease in trade payables		(30,000)
Interest paid (given in note (iv))		(92,000)
Income taxes paid		(working required)
Net cash from operating activities		<u>X</u>

## Operating Activities – April 2016 Q5

### Calculation of income taxes paid

Illustration using a T-Account

Insert the information given in the question i.e. balances at 2015 and 2016 and the expense for the year

Current Taxes Payable			
Bank (missing figure)	??????	Balance b/f 2015	60,000
Balance c/f 2016	<u>110,000</u>	Income tax expense (note (ii))	<u>80,000</u>
	<u>140,000</u>		<u>140,000</u>

## Operating Activities – April 2016 Q5

### Calculation of income taxes paid

Illustration using a T-Account

The 'missing figure' is the amount of tax paid

Current Taxes Payable			
Bank (missing figure)	30,000	Balance b/f 2015	60,000
Balance c/f 2016	<u>110,000</u>	Income tax expense (note (ii))	<u>80,000</u>
	<u>140,000</u>		<u>140,000</u>

## Operating Activities – April 2016 Q5

Insert the income tax expense and calculate net cash flow

Operating Activities		€
Profit before tax (given in note (i))		1,476,000
Add back depreciation		872,000
Add back loss on disposal (given in note (iii))		40,000
Add back interest expense (given in note (iv))		92,000
Increase in receivables		(160,000)
Increase in inventories		(100,000)
Decrease in trade payables		(30,000)
Interest paid (given in note (iv))		(92,000)
Income taxes paid		<u>(30,000)</u>
Net cash from operating activities		<u>2,068,000</u>

## Investing Activities – April 2016 Q5

- Let's start by inserting the information readily available in the question

Investing Activities	€	€
Cash received from disposal of assets	(working required)	
Cash paid for acquisition of assets	(working required)	
Interest received (none)	0	
Dividends received (none)	0	
<b>Net cash from investing activities</b>		<b><u>X/(X)</u></b>

## Investing Activities – April 2016 Q5

### Calculation of cash received from disposal of assets

- On 1 July 2016, the company sold PPE which originally had cost €1,000,000. On the date this PPE was sold, its carrying value was €600,000 and the firm made a loss on the sale of the PPE of €40,000.

Disposal Account			
Carrying value at disposal	600,000	Loss on disposal	40,000
	_____	<b>Bank (missing figure)</b>	<b><u>560,000</u></b>
	<u>600,000</u>		<u>600,000</u>

## Investing Activities – April 2016 Q5

Insert the cash received from disposal of assets

Investing Activities	€	€
Cash received from disposal of assets	560,000	
Cash paid for acquisition of assets	(working required)	
Net cash from investing activities		<u>X/(X)</u>

## Investing Activities – April 2016 Q5

### Calculation of cash paid to acquire assets

To calculate the cash paid to acquire assets (PPE), we can construct a T-account, inserting all of the information given in the question about movements in the carrying value of PPE for the year. The missing figure will be the cash paid.

PPE (Carrying Value)			
Balance b/f 2015	X	Disposal (carrying value)	X
Revaluation increase	X	Depreciation for year	X
Cash paid to acquire assets	?????	Balance c/f 2016	<u>X</u>
	<u>X</u>		<u>X</u>

## Investing Activities – April 2016 Q5

## Calculation of cash paid to acquire assets

	2016 €'000	2015 €'000	
<b>Non-Current Assets</b>			
Property, Plant & Equipment (PPE)	5,120	3,940	
Revaluation Surplus	120	80	
<b>PPE (Carrying Value)</b>			
Balance b/f 2015	3,940,000	Disposal (carrying value given in note (iii))	600,000
Revaluation increase	40,000	Depreciation (from operating activities workings)	872,000
<b>Cash paid to acquire assets</b>	<b>?????</b>	Balance c/f 2016	<u>5,120,000</u>
	<u>6,592,000</u>		<u>6,592,000</u>

## Investing Activities – April 2016 Q5

## Calculation of cash paid to acquire assets

	2016 €'000	2015 €'000	
<b>Non-Current Assets</b>			
Property, Plant & Equipment (PPE)	5,120	3,940	
Revaluation Surplus	120	80	
<b>PPE (Carrying Value)</b>			
Balance b/f 2015	3,940,000	Disposal (carrying value given in note (iii))	600,000
Revaluation increase	40,000	Depreciation (from operating activities workings)	872,000
<b>Cash paid to acquire assets</b>	<b><u>2,612,000</u></b>	Balance c/f 2016	<u>5,120,000</u>
	<u>6,592,000</u>		<u>6,592,000</u>

## Investing Activities – April 2016 Q5

Insert the cash paid for acquisition of assets and calculate net cash flow

Investing Activities	€	€
Cash received from disposal of assets	560,000	
<b>Cash paid for acquisition of assets</b>	<b>(2,612,000)</b>	
<b>Net cash from investing activities</b>		<b><u>(2,052,000)</u></b>

## Financing Activities – April 2016 Q5

- Let's start by inserting the information readily available in the question.

Financing Activities	€	€
Cash received from issue of equity	(working required)	
Cash received from borrowings	(working required)	
Cash paid for repayment of borrowings	(working required)	
Dividends paid	(working required)	
<b>Net cash from financing activities</b>		<b><u>X/(X)</u></b>



## Financing Activities – April 2016 Q5

### Calculation of cash received from issue of shares

- This is done by comparing the balance from the statement of financial position from 2015 to 2016 for share capital and share premium

	2016	2015	Increase
Share capital	240,000	200,000	Increase 40,000
Share premium	60,000	50,000	Increase 10,000

- Therefore, cash received from issue of shares €50,000

## Financing Activities – April 2016 Q5

- Insert the cash received from issue of shares.

Financing Activities	€	€
Cash received from issue of equity	50,000	
Cash received from borrowings	(working required)	
Cash paid for repayment of borrowings	(working required)	
Dividends paid	(working required)	
Net cash from financing activities		<u>X/(X)</u>

## Financing Activities – April 2016 Q5

### Calculation of cash received from issue of borrowings or cash paid to repay borrowings

- This is done by comparing the balance from the statement of financial position from 2015 to 2016 for long-term loans

	2016	2015	Increase/Decrease
Long-term loan	1,500,000	1,600,000	Decrease 100,000

- Therefore, cash paid to repay borrowings €100,000

## Financing Activities – April 2016 Q5

- Insert cash paid to repay borrowings.

Financing Activities	€	€
Cash received from issue of equity	50,000	
<b>Cash paid for repayment of borrowings</b>	<b>(100,000)</b>	
Dividends paid	(working required)	
<b>Net cash from financing activities</b>		<b>x</b>

## Financing Activities – April 2016 Q5

### Calculation of dividends paid

- This is done by comparing the increase or decrease in retained earnings to the profit after tax for the year. The difference, if any, is dividends paid.

	2016	2015	Increase/Decrease
Retained Earnings	3,798,000	2,402,000	1,396,000
Profit after tax (1,476,000 – 80,000 (note 2))			1,396,000

- Therefore, no dividends were paid during the year.

## Financing Activities – April 2016 Q5

- Calculate net cash flow.

Financing Activities	€	€
Cash received from issue of equity	50,000	
Cash paid for repayment of borrowings	(100,000)	
<b>Net cash from financing activities</b>		<b><u>(50,000)</u></b>

## Reconciling Cash & Cash Equivalents – April 2016 Q5

### Calculation of the increase or decrease in cash for the year

Statement of cash flows for year ended 31 December 2016		€
Net cash flow from operating activities		2,068,000
Net cash used for investing activities		(2,052,000)
Net cash flow from financing activities		<u>(50,000)</u>
<b>Decrease in cash for the year</b>		<b>(34,000)</b>
<b>Cash &amp; cash equivalents 1 January 2016</b>		
<b>Cash &amp; Cash equivalents 31 December 2016</b>		

The decrease in cash for the year can be reconciled to the difference between cash & cash equivalents at the beginning and end of the year

## Reconciling Cash & Cash Equivalents – April 2016 Q5

### Calculation of the cash & cash equivalents

This is done by comparing the balance of cash, bank, overdraft balances on each SOFP

	2016	2015
Cash & cash equivalents (from current assets on SOFP)	50,000	112,000
Bank overdraft (from current liabilities on SOFP)	<u>(32,000)</u>	<u>(60,000)</u>
Net cash & cash equivalents	<u>18,000</u>	<u>52,000</u>

The difference in cash & cash equivalents at the beginning and end of the year is a decrease of €34,000 i.e. reduced from €52,000 to €18,000.

# Reconciling Cash & Cash Equivalents – April 2016 Q5

## Insert cash & cash equivalent balances

Statement of cash flows for year ended 31 December 2016		€
Net cash flow from operating activities		2,068,000
Net cash used for investing activities		(2,052,000)
Net cash flow from financing activities		<u>(50,000)</u>
Decrease in cash for the year		(34,000)
Cash & cash equivalents 1 January 2016		<u>52,000</u>
Cash & Cash equivalents 31 December 2016		<u>18,000</u>

## Conclusion

### The key skills required to prepare a statement of cash flows are:

- Know the proforma layout of the statement of cash flows
- Understand the difference between the increase or decrease in cash and the profit or loss calculated on an accruals basis
- Don't miss the easy marks
- Practice the different techniques used to calculate the 'missing figures' (this really tests your understanding of double entry book-keeping)
- Best of luck!

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