



SIMPLE STEPS FOR THE PREPARATION OF FUNDS FLOW STATEMENT

Dr. L.
Subramanyam
Naidu*

M.Com, Ph.D, APSET, MBA (B&F), AP&TS SET, MBA (F), ICSI (FINAL), In-Charge Principal, Dr. R.C. REDDY DEGREE COLLEGE, R.C.ROAD, TIRUPATI. *Corresponding Author

ABSTRACT

A funds flow analysis helps in explaining how efficiently the management has used its working capital and also suggests ways to improve working capital position of the firm. Funds flow statement has to be used along with financial statements for inference of financial strengths and weakness of a company. So, funds flow statement is one of the best tools for analysis of financial statement. In this article I can explain simple steps for preparation of funds flow statement with the help of comparative balance sheet. It is very useful to students and scholars.

KEYWORDS : Analysis of Financial Statement – Funds Flow Statement – Working Capital.

INTRODUCTION

The 'funds' ordinarily means cash and wealth, but here it means cash in short term and working capital in long term. This is why; the term fund is used as 'cash' in cash flow analysis and as 'working capital' in funds flow analysis. The concept of funds includes the following:

- **Literal Cash:** This includes cash in hand and demand deposits in banks.
- **Short-Term Monetary Assets:** These include marketable securities.
- **Net Monetary Assets:** These are the net quick assets less short-term payables.
- **Working Capital:** The difference between current assets and current liabilities.

Funds flow indicates the flow of working capital between two points of time. It involves information relating to the various transformations undergone by working capital (i.e. the changes that have taken place in working capital) during the period involved between the two points of time.

Funds flow analysis is a statement showing sources and uses of funds for a period of time.

According to Anthony, "The funds flow statement describes the sources from which additional funds were derived and the use to which these sources were put".

The statement, which is prepared to show the inflow (sources) and outflow (uses or application) of fund, is termed as "Funds Flow Statement".

Finally a funds flow statement is a consolidated statement of all cross transactions.

When There Is A Flow Of Fund?

There is a flow of fund in case of all cross transactions. Cross Transactions i.e. transactions involving a current account and a non-current account bring about a change in the fund or working capital.

For example: Purchase of Asset for cash: In this transaction there are two accounts one is Asset Account (Non-Current Account) and other Cash account (Current Account), so here the effect of this transaction is decrease in cash that leads to decrease in fund or working capital. So, we can say there is a flow of fund.

There is no flow of fund in case of all non-cross transactions. Non-cross Transactions i.e. transactions involving a current account and current account or non-current account and non-current account does not bring any change in the fund or working capital.

For example: Cash collected from debtors: In this transaction there are two accounts, one is Debtors Account (Current Account) and other Cash account (Current Account), so here the effect of this transaction is increase in cash and decrease in debtors, it does not affect the fund or working capital. So, we can say that there is no flow of fund.

For example: Purchase of Asset for consideration by issue of shares: In this transaction there are two accounts, one is Asset Account (Non-Current Account) and other Share Capital account (Non-Current Account), so here the effect of this transaction is increase in Share Capital and increase in asset, it does not affect the fund or working capital. So, we can say that there is no flow of fund.

Balance Sheet

Liabilities	B.Y	C.Y	Assets	B.Y	C.Y
Share Capital	xx	xx	Building	xx	xx
Reserves	xx	xx	Machinery	xx	xx
P&L A/c	xx	xx	Goodwill	xx	xx
Debentures	xx	xx	Investments	xx	xx
Bank Loans	xx	xx	Stock	xx	xx
Creditors	xx	xx	Debtors	xx	xx
Bills Payable	xx	xx	Bills receivables	xx	xx
Bank O.D	xx	xx	Cash in hand	xx	xx
Provisions for taxation	xx	xx	Cash at bank	xx	xx
Proposed Dividend	xx	xx	O/s incomes	xx	xx
O/s expenses	xx	xx	Preliminary exp.	xx	xx

B.Y: Base Year or Last Year; **C.Y:** Current Year

PREPARATION OF FUNDS FLOW STATEMENT**Step: 1 Statement Showing Changes In Working Capital**

It is prepared with the help of only current assets and current liabilities. After preparing this statement, we can find either "Increase in working capital" or "Decrease in working capital". The following transactions are affecting the working capital.

- Increase in Current Assets in current year when compared to last year: Increase in Working Capital
- Decrease in Current Assets in current year when compared to last year: Decrease in Working Capital
- Increase in Current Liabilities in current year when compared to last year: Decrease in Working Capital
- Decrease in Current Liabilities in current year
- when compared to last year: Increase in Working Capital

If there is an Increase in Working Capital – Transfer to Funds flow statement "Application of Fund" side
If there is a Decrease in Working Capital – Transfer to Funds flow statement "Source of Fund" side

Step: 2 Calculations of Funds From Operations or Funds Lost in Operations

We can prepare "Adjusted Profit & Loss Account" with the help of some components of Balance sheet and given adjustments. After preparing adjusted profit and loss account we can find either "Funds from operations" or "Funds lost in operations". With the help of following transactions we can prepare this account.

Profit & Loss Account

- Last Year P&L A/c shown as Opening Balance in adjusted profit & loss account Cr. Side.
- Current Year P&L A/c shown as Closing Balance in adjusted profit & loss account Dr. Side

Reserves

- Increase in reserves in current year when compared to last year, it is treated as "transfer to reserves" and shown in Dr. side of adjusted profit & loss account.
- Decrease in reserves in current year when compared to last year, it is treated as "transfer from reserves" and shown in Cr. side of adjusted profit & loss account.

Provision For Taxation (given In Adjustments)

- It is treated as non-current liability, if any provisions made during the year shown in Dr. side of adjusted profit & loss account

Proposed Dividend (Given In Adjustments)

- It is treated as non-current liability, dividend proposed during the year shown in Dr. Side of adjusted profit & loss account.
- Dividend received during the year shown in Cr. Side of adjusted profit & loss account.

Interim Dividend (Given In Adjustments)

- It is treated as non-current liability, interim dividend declared by board of directors shown in Dr. side of adjusted profit & loss account.

Depreciation On Fixed Assets

- It is shown in Dr. side of adjusted profit & loss account

Appreciation On Fixed Assets

- It is shown in Cr. Side of adjusted profit & loss account

Loss On Sale Of Fixed Assets

- It is shown in Dr. side of adjusted profit & loss account

Profit On Sale Of Fixed Assets

- It is shown in Cr. Side of adjusted profit & loss account

Intangible And Fictitious Assets

- If there is any decrease in the value of intangible and fictitious assets in current year when compared to last year, it is treated as "intangible or fictitious assets written off". It shown in Dr. side of adjusted profit & loss account.

Finally

- If there is a balancing figure in debit side of adjusted profit & loss account it is treated as "Funds lost in Operations"
- If there is a balancing figure in credit side of adjusted profit & loss account it is treated as "Funds from Operations"

Step: 3 Preparation Of Funds Flow Statement

It is a statement prepared at the end of the financial year indicating sources of funds and applications of funds. It is prepared with the help of the following transactions.

Share Capital

- Increase in share capital in current year when compared

to last year is treated as "issue of share capital" shown in sources of fund side.

- Decrease in share capital in current year when compared to last year is treated as "redemption of share capital" shown in application of fund side.

Debentures

- Increase in debentures in current year when compared to last year is treated as "issue of debentures" shown in sources of fund side.
- Decrease in debentures in current year when compared to last year is treated as "redemption of debentures" shown in application of fund side.

Loans

- Increase in loans in current year when compared to last year is treated as "raising of loans" shown in sources of fund side.
- Decrease in loans in current year when compared to last year is treated as "repayment of loan" shown in application of fund side.

Fixed Assets & Investments

- Increase in fixed assets and investment in current year when compared to last year is treated as "purchase of fixed assets and investments" shown in applications of fund side.
- Decrease in fixed assets and investment in current year when compared to last year is treated as "sale of fixed assets and investments" shown in sources of fund side.

Intangible Fixed Assets

- Increase in intangible fixed assets in current year when compared to last year is treated as "purchase of Intangible fixed assets" shown in applications of fund side.

Proposed Dividend (Given In Adjustment)

- It is treated as non-current liability, last year proposed dividend shown in applications of fund side.

Interim Dividend (Given In Adjustment)

- It is treated as non-current liability and interim dividend

- ❖ If there is a Funds lost in operations – Transfer to Funds flow statement "Applications of Fund" side
- ❖ If there is a Fund from operations – Transfer to Funds flow statement "Sources of Fund" side

Non-trading Payments

- Non trading payments like interest paid, dividends paid shown in applications of fund side.

Non-trading Receipts

- Non-trading receipts like interest received, dividends received shown in sources of fund side.

REFERENCES:

1. R.S.N. PILLAI & BAGAVATHI, Management Accounting
2. M.Y Khan & PK Jain, Management Accounting
3. I.M Pandey, Management Accounting.