

Query No. 5

Subject: Presentation of accrued interest in the Statement of Cash Flows.¹

A. Facts of the Case

1. A Corporation is a Central Public Sector Undertaking (CPSU) under the Administrative Ministry of Social Justice and Empowerment and is registered under section 25 of Companies Act, 1956 (Now section 8 of the Companies Act, 2013).

2. The querist has stated that the financial statements of the Corporation are being prepared as per Indian Accounting Standards (Ind ASs) as applicable from the financial year (F.Y.) 2018-19. The accounts of the Corporation are subject to audit by the statutory auditors appointed by the Comptroller and Auditor General (C&AG) of India under section 139(5) of the Companies Act, 2013 (hereinafter referred as 'the Act'). The statutory auditors are responsible for expressing opinion on the financial statements under section 143 of the Act, based on the independent audit in accordance with the standards on auditing prescribed under section 143(10) of the Act. C&AG is required to conduct supplementary audit under section 143(6)(a) of the Act and give its report.

3. The querist has further stated that the Corporation prepares its statement of cash flows as per indirect method. The Corporation has invested its saving/liquid assets in fixed deposit and gained interest of Rs. 2405.54 lakh during the F.Y. 2020-21 on accrual basis. An amount of Rs. 2244.75 lakh has been credited in its bank account against such gain and Rs. 160.79 lakh (net) accrued during the F.Y. 2020-21. The working of net accrued interest, as given in Note No. 7.01 of balance sheet (F.Y. 2020-21) is as follows:

Particulars	Amount (Rs. In Lakh)
Accrued Interest for the F.Y. 2020-21	696.30
Accrued Interest for the F.Y. 2019-20	535.51
Net Accrued Interest	160.79

4. The querist has also stated that for the presentation of above-mentioned interest amount, the Corporation deducted Rs. 2405.54 lakh from the profit to reach the actual cash flows from operating activities and the same amount is also shown in cash inflows from investing activities as per the past practices of the Corporation and statutory auditor is also satisfied with this presentation. Also, in many Central Public Sector Enterprises (CPSEs), the same procedure is followed for the presentation of interest received in the statement of cash flows.

5. According to the querist, it is pertinent to mention that there is no standard format in Schedule III to the Companies Act, 2013 for presentation of statement of cash flows but it refers to follow Indian Accounting Standard (Ind AS) 7 for presentation of statement of cash flows.

6. C&AG, while conducting supplementary audit, issued an audit memo regarding the presentation of interest amount received by the Corporation and pointed out as follows:

¹ Opinion finalised by the Committee on 11.4.2022.

- i. As per paragraph 31 of the Ind AS 7, 'Statement of Cash Flows', "interest and dividends received should be classified as cash flows from investing activities".
- ii. The interest received by the Corporation during the year 2020-21 was Rs. 2244.75 lakh; however, the same has been incorrectly depicted as Rs. 2405.54 lakh in cash flows from investing activities due to non-adjustment of accrued interest. Further, the cash outflow due to increase in accrued interest of Rs. 160.79 lakh has incorrectly been included in cash flows from operating activities.
- iii. This resulted in understatement of cash flows from operating activities and overstatement of cash flows from investing activities by Rs. 160.79 lakh.

7. The impasse was resolved after resolving to approach the Expert Advisory Committee (EAC) of the Institute of Chartered Accountants of India for its opinion.

B. Query

8. On the basis of the above, the querist has sought the opinion of the Expert Advisory Committee (EAC) on continuance/discontinuance of presentation of interest received on accrual basis, in the statement of cash flows.

C. Points considered by the Committee

9. The Committee notes that the basic issue raised in the query relates to presentation of accrued interest receivable in the statement of cash flows, prepared in accordance with Indian Accounting Standard (Ind AS) 7, 'Statement of Cash Flows'. The Committee has, therefore, considered only this issue and has not examined any other issue that may arise from the Facts of the Case, such as, accounting for interest (including accrued interest) for financial year 2019-20 and 2020-21, presentation of cash flows arising from taxes on interest income, etc. Further, the Committee, while expressing its opinion, has presumed that investment in fixed deposits is not part of cash and cash equivalents of the Corporation.

10. The Committee notes that the Corporation in the extant case is preparing its statement of cash flows as per indirect method. The Corporation has invested its savings in fixed deposit and gained interest of Rs. 2405.54 lakh during F.Y. 2020-21 including interest accrued but not received of Rs. 160.79 lakh. The Corporation deducted Rs. 2405.54 lakh from the profit to reach the actual cash flows from operating activities and the same amount is also shown in cash flows from investing activities.

In this regard, the Committee notes the following paragraphs of Ind AS 1, 'Presentation of Financial Statements' and Ind AS 7, 'Statement of Cash Flows':

Ind AS 1

"27 An entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting."

Ind AS 7

"Objective

...

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.”

“Cash flows are inflows and outflows of cash and cash equivalents.”

From the above, the Committee notes that the statement of cash flows as per the requirements of Ind AS 7 is essentially a statement of changes in cash and cash equivalents and that the cash flow information is not provided based on the accrual basis of accounting. Thus, an item of income and expenses recognised on accrual basis of accounting in the Statement of Profit and Loss and balance sheet will not become part of changes in cash flows unless it represents changes in cash and cash equivalents during the reporting period.

11. The Committee also notes the following requirements of Ind AS 7:

“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.”

“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 should be classified as cash flows arising from operating activities. In the case of other entities, cash flows arising from interest paid should be classified as cash flows from financing activities while interest and dividends received should be classified as cash flows from investing activities. Dividends paid should be classified as cash flows from financing activities.”

“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 lease;
- (b) the acquisition of an entity by means of an equity issue; and
- (c) the conversion of debt to equity.”

From the above, the Committee notes that in the case of entities (other than financial institutions), cash flows arising from interest received should be classified as cash flows from investing activities. Further, investing transactions (interest received in the extant case) that do not require use of cash or cash equivalents shall be excluded from the statement of cash flows. The Committee further notes that under indirect method of preparation of statement of cash flows, profit or loss is adjusted for the effects of items for which the cash effects are investing and then while presenting cash flows from investing activities, non-cash transactions are excluded.

In this context, the Committee notes that in the extant case, out of total interest income amounting to Rs. 2405.54 lakh, net accrued interest for the reporting period is Rs. 160.79 lakh, which is a non-cash transaction, i.e. not received in the form of cash or cash equivalent. Therefore, this portion of accrued interest which is non-cash should be excluded from the cash flows from investing activities while presenting the statement of cash flows as there is no cash inflow during the current reporting period. However, under indirect method, while adjusting the profit or loss for the effects of items for which cash effects are investing, the amount to be adjusted would be total interest income during the reporting period (i.e. including accrued interest) as the total effect of the investing transaction is to be nullified from the net profit under the cash flows from operating activity. Accordingly, on the basis of above-mentioned requirements, the Committee is of the view that the inclusion of accrued interest amounting to Rs. 160.79 lakh, under the cash flows from investing activities in the statement of cash flows of the Corporation, is not correct.

D. Opinion

12. On the basis of the above, the Committee is of the view that the inclusion of accrued interest amounting to Rs. 160.79 lakh, under the cash flows from investing activities in the statement of cash flows of the Corporation, is not correct, as discussed in paragraphs 10 and 11 above.
