

1. Would redemption of debentures result in inflow, outflow or no flow of cash? Give your answer with reason.

ANS. Outflow of cash because cash goes out.

2. Under which class of activity, would you put 'proceeds from sale of buildings' while preparing the cash flow statement?

ANS. Investing activity.

3. Would 'sale of marketable securities at par' result in inflow, outflow or no flow of cash? Give your answer with reason.

ANS. No flow of cash as marketable securities are cash equivalents.

4. Under which type of activity would you classify computer purchased for cash while preparing the cash flow statement?

ANS. Investing activity.

5. Would declaration of final dividend result in inflow, outflow or no flow of cash? Give your answer with reason.

ANS. No flow of cash. Payment of dividend, and not declaration of dividend, causes outflow of cash.

6. Under which type of activity would you classify 'issuing 10% debentures' while preparing the cash flow statement?

ANS. Financing activity.

7. State whether payment of cash to creditors will result in inflow, outflow or no flow of cash.

ANS. Outflow of cash.

8. State with reason whether conversion of debentures into equity shares by a finance company will result in inflow, outflow or no flow of cash.

ANS. No flow of cash because it is a non-cash item.

9. Under which type of activity will you classify 'commission and royalty received' while preparing cash flow statement?

ANS. Operating activity.

10. Give an example of the activity which remains financing activity for every enterprise.

ANS. Payment of dividend on shares.

11. State with reason whether 'purchase of a fixed asset on long-term deferred payment' would result in inflow, outflow or no flow of cash.

ANS. No flow because it does not involve cash.

12. Under which type of activity would you classify 'refund of income tax received' while preparing a cash flow statement?

ANS. Operating activity.

13. While preparing a cash flow statement, what type of activity is payment of cash to acquire shares of another company by (i) a trading company and (ii) an investment company?

ANS. (i) Investing activity and (ii) Operating activity.

14. While preparing cash flow statement what type of activity is payment of cash to acquire debentures' by (i) an investment company and (ii) trading company?

ANS. (i) Operating activity; (ii) Investing activity.

15. State with reason whether deposit of cash into bank will result into inflow, outflow or no flow of cash.

ANS. Deposit of cash into bank does not result in inflow or outflow of cash because there is no change in 'cash'. Cash includes both cash in hand and at bank.

16. Under which class of activity would you put interest received on debentures while preparing the cash flow statement of a manufacturing company?

ANS. Investing activity.



17. The accountant of RVS Ltd. while preparing cash flow statement added depreciation provided on fixed assets to net profit for calculating cash flow from operating activities. Was he correct in doing so? Give reason.

ANS. He is correct because depreciation is a non-cash expense.

18. While preparing the cash flow statement, the accountant of AKG Ltd. showed dividend paid under operating activities. Was he correct in doing so? Give reason.

ANS. He is not correct because payment of dividend is a financing activity.

19. Dividend paid by a financial company is classified under which type of activity while preparing a cash flow statement?

ANS. Financing activity (Note : Payment of dividend is a financing activity for all types of concerns).

20. Under which type of activity will you classify 'interest paid on long-term borrowings' while preparing the cash flow statement?

ANS. Financing activity.

21. State with reason whether 'discount received on making payment to suppliers' would result in inflow, outflow or no flow of cash.

ANS. Discount received on payment to suppliers does not result in inflow of cash because it does not involve cash.

22. Under which class of activity will you put 'proceeds from sale of machinery' while preparing the cash flow statement?

ANS. Investing activity.

23. Why is depreciation added to income from operations in a formal cash flow statement?

ANS. Depreciation is added to income from operations because depreciation is not a cash expense.

24. Why are only the non-cash accounts examined when it is the cash account that is being explained in a cash flow statement?

ANS. Non-cash accounts are examined because any change in cash must, at the same time, affect some other account.

25. Name three sources of cash other than those from normal operations.

ANS. Proceeds from issue of shares, borrowing money by issue of debentures or otherwise, selling fixed assets.

26. Name three uses of cash other than for normal operations.

ANS. Buying fixed assets, redemption of debentures, payment of dividend.

27. A company issues for cash 10,000 equity shares of ₹ 10 each at a premium of ₹ 2 per share and ₹ 50,000 debentures at par to a vendor as consideration for purchase of machinery. State in each case the amount of cash flow and the class of activity under which it falls.

ANS. Proceeds from issue of equity shares ₹ 1,20,000 is cash inflow from financing activities. Issue of debentures for consideration other than cash does not result in any flow of cash.

28. State with reason whether charging depreciation on furniture would result in inflow, outflow or no flow of cash.

ANS. No flow of cash because it is a non-cash expenditure.

29. State with reason whether cash withdrawn from bank for office use would result in inflow, outflow or no flow of cash.

ANS. No flow of cash because cash comprises cash in hand and cash at bank, and consequently, cash itself cannot be a cause for inflow or outflow of cash.

30. List any two investing activities which result into outflow of cash.

ANS. (1) Purchase of machinery ; (2) Purchase of investments.



31. List any two financing activities that will result into outflow of cash.

ANS. (1) Redemption of debentures ; (2) Payment of dividend on shares.

32. Give one transaction which may result into outflow of cash and one which may result into no flow of cash.

ANS. Outflow of cash : Redemption of preference shares.

No flow of cash : Redemption of debentures by conversion into equity shares.

33. Under what types of activity will you classify 'proceeds from sale of machinery' while preparing a cash flow statement ?

ANS. Investing activity.

34. List any one use of a cash flow statement.

ANS. It enables the management to account for a situation when the business has earned a good amount of profit and yet runs short of funds or when it has suffered a loss and still has a large cash balance.

35. Why do companies prepare a cash flow statement ?

Or

What purpose does a cash flow statement serve ?

ANS. A company prepares a cash flow statement to show under specific heads the various sources from which cash flows in, the various purposes for which cash flows out and the net increase or decrease in cash and cash equivalents.

36. State any one objective of preparing a cash flow statement.

ANS. To provide information regarding inflow and outflow of cash and cash equivalents during an accounting period specifically from operating, investing and financing activities of an enterprise.

37. When does a flow of cash arise ?

Or

What do you mean by 'flow of cash' ?

ANS. The term 'flow' means change. So, the term flow of cash means 'change in cash and cash equivalents'. A flow of cash arises when a transaction either increases or decreases the cash and cash equivalents of a concern.

38. Define cash, cash equivalents and cash flows as per AS-3.

ANS. Cash comprises cash on hand and demand deposits with banks. Cash equivalents are short-term highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value. Cash flows are inflow and outflow of cash and cash equivalents.

39. How are the various activities classified according to AS-3 (Revised) while preparing a cash flow statement ?

ANS. Various activities are classified into : (1) Operating activities ; (2) Investing activities ; and (3) Financing activities.

40. State the major classification of cash flows as per AS-3.

ANS. (i) Cash flows from operating activities ; (ii) Cash flows from investing activities ; and (iii) Cash flows from financing activities.

41. What do you mean by operating activities ?

ANS. Operating activities are the principal revenue producing activities of the enterprise and other activities that are not investing or financing activities.

42. What do you mean by investing activities ?

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

43. What do you mean by financing activities ?

ANS. Financing activities are activities that result in changes in the size and composition of the owners' capital and borrowings of the enterprise.



44. Give three examples of cash flows from operating activities.

ANS. (i) Cash receipts from the sale of goods and the rendering of services. (ii) Cash receipts from royalties, fees, commission and other revenue. (iii) Cash payments to suppliers of goods and services.

45. How is payment of income tax treated in a cash flow statement ?

ANS. Payment of income tax is an outflow of cash, classified under operating activities and shown as a separate item.

46. Why is ignoring non-cash items a limitation of the cash flow statement ?

ANS. Since a cash flow statement ignores non-cash items, net cash flow does not necessarily mean net income of the business. It fails to disclose some significant information like acquisition of assets by issue of shares/debentures or the conversion of debentures into shares and so on.

47. What is meant by cash equivalents ?

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

48. State whether depreciation charged by a company will result in inflow, outflow or no flow of cash.

ANS. No flow of cash.

49. Interest paid by an investment company will come under which activity while preparing a cash flow statement ?

ANS. Interest paid by an investment company (being a financial enterprise) should be classified as cash flow from operating activities.

50. Dividend paid by a manufacturing company is classified under which kind of activity while preparing a cash flow statement ?

ANS. Dividend paid should always be classified as cash flow from financing activities.

51. List any two items of operating activities that are typical of and pertaining to electronic media.

ANS. (1) Advertisement revenue received. (2) Salaries paid to technicians.

52. When is dividend received considered as operating activity ?

ANS. In case of financial enterprises, cash inflows arising from dividend received are considered as cash flows from operating activities.

53. State why non-cash transactions are ignored while preparing a cash flow statement.

ANS. A cash flow statement is prepared following the cash basis accounting. It shows inflows and outflows of cash and cash equivalents only. Hence non-cash transactions are ignored.

54. When is interest received considered as financing activity ?

ANS. Cash inflow arising from interest received is never considered as cash flow from financing activities.

55. State whether payment of cash to creditors will result in inflow, outflow or no flow of cash.

ANS. Outflow of cash.

56. Dividend paid by a finance company is classified under which kind of activity while preparing a cash flow statement ?

ANS. Dividend paid is classified as a financing activity. It does not matter whether it is a financial or non-financial enterprise.

57. State whether conversion of debentures into equity shares by a financing company will result in inflow, outflow or no flow of cash.

ANS. No flow of cash (irrespective of whether the company is a financial or non-financial enterprise).