

Solution:

The table is filled with values to answer (1) and (2).

TABLE FOR PROBLEM 8-61 (Amount in \$ in thousands)				
Particulars	1. Zero Income Tax		2. 40% Income Tax	
	Straight Line	Accelerated	Straight Line	Accelerated
Revenues (all cash)	950	950	950	950
Cash operating expense	600	600	600	600
Cash provided by operation before tax	350	350	350	350
Depreciation Expense	100	60	100	60
Pre-tax Income	250	290	250	290
Income Tax	0	0	100	116
Net Income	250	290	150	174
Supplementary Analysis:				
Cash provided by operation before tax	350	350	350	350
Income Tax	0	0	100	116
Cash provided by operations	350	350	250	234

(3) No, depreciation does not provide cash, as with zero tax, any of the two-depreciation method used results in the same cash flow. The difference occurs due to income tax, which shows that the depreciation helps to reduce income tax, and this accounts for its apparent way of “earning cash”.

(4) All decreased by \$16.

(5) There will be no effect of this on the cash flow, because depreciation does not affect cash flow at all. It is a non-cash expense, so it has no effect.