EBITDA ignores a real cost

Letters: 2000, 2002 · Difficulty: Intro

> *"References to EBITDA make us shudder — does management think the tooth fairy pays for capital expenditures?" (2000)*

1. Net income $50, interest $10, income taxes $20, depreciation and amortization $30. What is EBITDA?
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2. Why does Buffett call depreciation a real cost even though it is a "non-cash" expense?

   A. Depreciation is a liability

   B. The cash was paid up front when the asset was bought

   C. Depreciation is paid in cash every year

   D. Depreciation increases taxes owed

Source: Warren E. Buffett, Letters to Berkshire Hathaway Shareholders: 2000, 2002 (berkshirehathaway.com/letters). Quotation © Berkshire Hathaway Inc., all rights reserved; quoted for non-commercial teaching. Numbers in the questions are made up unless stated.