**Unit 9: Depreciation and amortization**

“When you climb a hill, all what you find, is numbers of hills to be climbed”

Nelson Mandela, 1918-2013, Former President of South Africa.

A company's assets are usually divided into **current assets** like cash and stocks or inventory, which will be used or converted into cash in less than a year; and **fixed** **assets** such as building and equipment, which will continue to be used by the business for many years. However, fixed assets wear out of date (become unusable or obsolete), and eventually have little or no value. Consequently, fixed assets are depreciated; their value on the balance sheet is reduced each year by a charge on the profits and loss. In other words, part of the cost of the asset is deducted from the profit each year.

The whole cost of the asset will be charged during all the years it is used, this is the **accounting system depreciation**.

Land is usually not depreciated, it tends to appreciate or gain in value. British companies usually revalue (calculate a new value for) appreciating fixed assets. The revaluation is at either **current replacement cost** – how much it would cost to buy new ones – or at **net realizable value** (NRV) – how much they could be sold.

Appreciation is recorded only in countries that use **inflation accounting systems**. Companies in countries, which use **historical cost system** – recording only the **original purchase price** of asset –, do not usually record an **estimated market value** (the price at which something could be sold today). The conservatism and objectivity principles support this.

The most common depreciation system of fixed assets is the **straight-line method**, which means charging equal annual amounts against profits during the lifetime of the asset (e.g. : deducting 10 % of an asset's value from the profits every year for 10 years). Many European countries allow **accelerated depreciation**, businesses can deduct the whole cost of an asset in a short time. Accelerated depreciation allowances are an incentive to investment: a way to encourage it. If a company deduces the entire cost of an asset in a single year, it reduces its profits and therefore the amount of taxes it has to pay.

**Comprehension**:

1. What is the difference between fixed and current assets?
2. Are stocks considered as fixed assets?
3. Are companies allowed to appreciate the value of their assets? How is that?
4. Explain how can the law encourages companies to investment.
5. According to which principles, countries use the historical cost system?
6. How companies can depreciate their assets ?

**Vocabulary**:

Exercise 1: match each word with its appropriate definition.

Appreciate – obsolete – current assets – revalue – fixed assets – wear out

* 1. To record something at different price.
  2. Assets that will no longer be in the company in 12 months’ time.
  3. To increase rather than decrease in value.
  4. Out of date, needing to be replaced by something newer.
  5. Assets that will remain in the company for several years.
  6. To become used and damaged.

Exercise 2: match the items in **A** with the verbs in **B** to have word combinations, and then use some of the word combinations to complete sentences below.

**A**: costs – administrative expenses - fixed assets – market value – purchase price

**B :** - deduce –depreciate- record- reduce- estimate

- To calculate profit, we ……………………………. from the turnover.

- Managers should ……………………………. to achieve company’s target.

- Companies choose straight-line method to ……………………………….

- Accountants do not …………………………. to ………………………….

- Because land usually appreciates, companies ………………… its ……………………… on the balance sheet.

Exercise 3: match the two parts of sentences

1. All fixed assets can appreciate if there is high inflation.

2. Accelerated depreciation allows companies to

3. Fixed assets generally lose value, except for land

4. The straight-line method of depreciation

5. Accelerated depreciation reduces companies’ tax bills

a. which usually appreciate.

b. charges equal amounts against profits every year.

c. remove some extremely valuable assets from their balance sheet.

d. which encourages them to invest in new factories.

e. However, with the historical cost accounting, this fact is not considered.

**Grammar***: The present perfect tense*

1. Present perfect form: the present perfect of any verb is composed of two parts :

The ***auxiliary verb to have*** (present tense) + ***the past participle*** of the main verb.

The past participle of a regular verb is ***base + ed***. For irregular verb, we refer to the table of irregular verbs.

Negative form: Subject + to have + not + past participle.

Interrogative form: to have + Subject + past participle

E.g., she ***has arrived;*** I ***have taken***…. They ***have not finished*** yet, ***have*** you ***visited*** the museum?

1. Present perfect function :

The present perfect is used to indicate a link between the present and the past. The time of the action is before now but not specified. The present perfect is used in the following cases :

|  |  |
| --- | --- |
| Cases | Examples |
| An action or situation that started in the past and continues in the present. | I have lived in Boumerdes since 1985. (and I still do) |
| An action performed during a period that has not finished yet. | She has been in the cinema twice this week. (and the week isn't over yet) |
| A repeated action in an unspecified period between the past and now. | They have visited Portugal several times. |
| An action that was completed in the very recent past. (expressed by just) | I have just finished my work. |
| An action when the time is not important. Only matter the results of the action. | She has read « War and peace ».  He has learnt English, Russian and French. |