

Capital Expenditure

Under standard accounting practices local authorities are required to account for revenue expenditure and capital expenditure differently. Capital expenditure is defined in the Local Government 2003 Act as expenditure which, in accordance with proper accounting practices, falls to be capitalised. Proper accounting practice is currently accepted to be the CIPFA/ LASAAC Code of Practice on Local Authority Accounting: A Statement of Recommended Practice (known as the SORP).

Generally speaking capital expenditure results in a fixed asset which is reported separately in the Council's account from other expenditure. On this basis, capital expenditure essentially relates to the provision and improvement of significant fixed assets including land, buildings and equipment (such as schools, new houses and machinery) which will be of use or benefit in providing services for more than one financial year.

However, in practical terms, it is often quite difficult to easily distinguish between capital and revenue expenditure and as such there are a number of ways that we should consider expenditure in order to identify what is capital and what is revenue.

Revenue expenditure is expenditure incurred for the purpose of the organisations daily activity, services or to maintain fixed assets. For example employees pay, travel expenses and IT consumables are all deemed to be revenue expenditure.

The common definition of capital expenditure is

“Capital expenditure is expenditure that results in the acquisition or construction of a fixed asset (land, building, vehicle, equipment) or enhancement of an existing fixed asset.”

Determining the acquisition or construction of a new asset is relatively straight forward and as such the greatest difficulty is often associated with identifying expenditure that can be said to enhance an existing asset.

To be an enhancement, the work undertaken must either

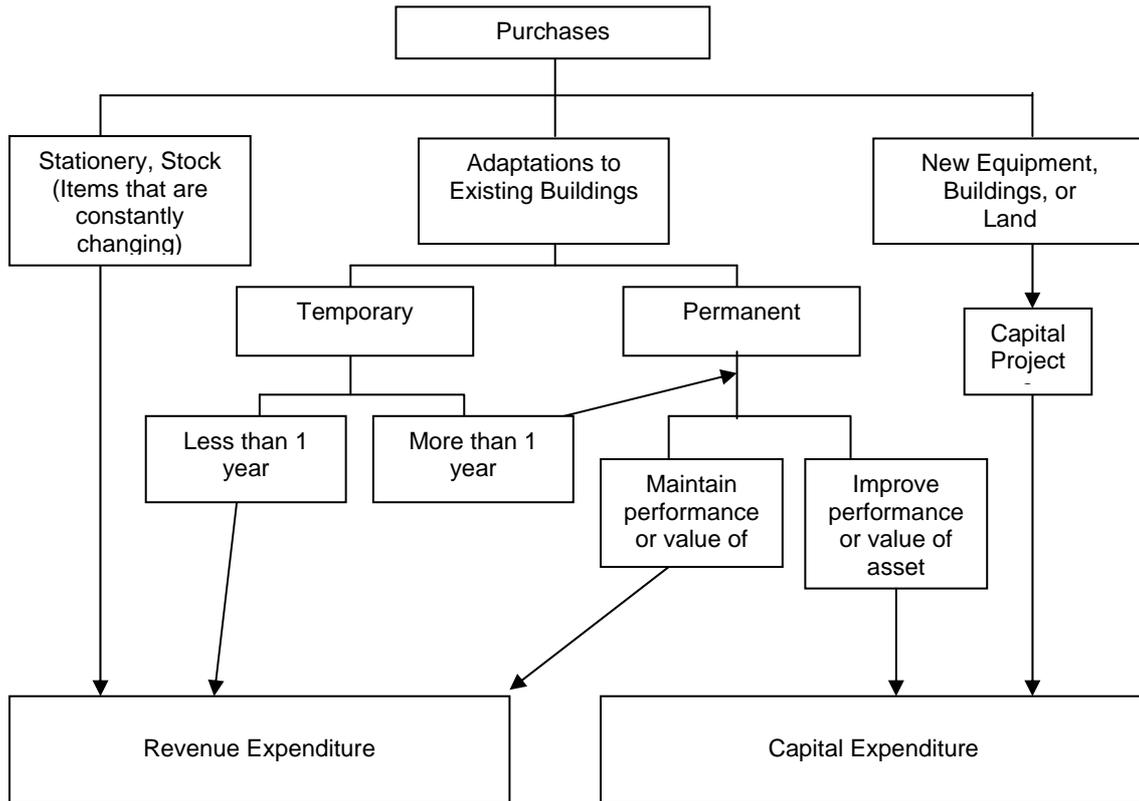
- **Lengthen substantially the useful life of the asset** – beyond the current assessment of the useful life of the asset. For example, the assessment would usually assume that a property would always have an effective paint coverage and therefore painting would only ensure that the property remained useful for the period originally anticipated. In contrast, the assessment might assume that the property will continue to have a flat roof in good repair. Its subsequent replacement with a pitched roof will be more effective at protecting the building from degradation by the elements and should result in a more optimistic assessment of the prospective useful life.
- **Increase substantially the market value of the asset** – if the asset were valued after the works substantially higher than prior to the works.
- **Increase substantially the extent to which the asset can or will be used for the purpose of or in conjunction with the functions of the authority** – for example extending a building to provide a wider service or making a building fit for a purpose that it would not otherwise be fit for.

Some other issues to bear in mind are

- Expenditure on loans and grants to other parties for capital purposes or expenditure to enhance an asset owned by a third party can also be capital.
- For reasons of materiality and consistency with other capital controls, de minimis levels are applied, below which expenditure is treated as revenue. These de minimis levels are set at £2,000. This level should be applied at scheme/project level rather than on an invoice-by-invoice basis.
- If treated singly, an asset may fall below the capitalisation threshold. Several small value assets of a similar nature may be purchased at once, for example as part of the same project. If so, it is the value of the purchase of all the assets that determines whether expenditure falls above or below this threshold. For example, a new chair costing £300, would be revenue expenditure; whereas a programme of replacing all the chairs in a particular building would be capital expenditure. The question of grouping typically applies to the purchase of information technology, other equipment or office furniture.
- The purchase or creation of a capital asset might require a department to undertake other expenditure necessary to procure and commission the asset. Such internal costs will include employees salaries and expenses arising directly from the construction and acquisition of the specific fixed asset. These costs, and only those costs attributable to bringing the asset into working condition, should be recorded as capital expenditure.
- Costs incurred in the early stages of a project to acquire or create a capital asset should only be recorded as capital if at the time they are incurred there is a clearly defined project, the costs are separately identifiable and it is reasonably certain that the project will be completed and will result in an asset that will eventually be brought into use.
- Capital expenditure includes any architects or surveyors fees where that are an integral part of, and specific to, the acquisition or the construction of a building. This also applies to consultancy costs in procuring other capital assets.
- Expenditure on consultancy to help decide whether a capital acquisition or project should go ahead is revenue expenditure.
- **ICT** – Purchase of new computer equipment, associated infrastructure and software may be treated as a capital cost. Software licences may be charged only if it is a permanent licence. The Local Government Act 2003 allows computer software to be capitalised only where the use of the software is granted for a period of at least 1 year. Annual licences or subscription charges are not allowed and must be treated as revenue expenditure.
- Maintenance contracts associated with new hardware/software acquisitions can only be capitalised for the first year of the project, where the costs are deemed to be inclusive of the capital scheme. The cost associated with ongoing maintenance or support contracts after the first year should be met from revenue expenditure.

The flow chart attached may be helpful in confirming the nature of expenditure – capital or revenue.

Capital or Revenue Expenditure



Distinguishing between expenditure on existing assets that maintains the use or value of that asset and expenditure that improves use or value can be difficult and judgement will always be required. The following key words can be indicators of whether expenditure is more likely to be Capital or Revenue expenditure.

Key words indicating Capital expenditure	Key words indicating Revenue expenditure
Enhance Upgrade Extend Improve Construct Purchase	Repair Maintain Replace Like-for-like Remedial Renew

The following page gives some examples of the most common expenditure on existing assets and whether it should be treated as capital or revenue.

**Examples of Capital and Revenue Expenditure
Summary Explanation**

Capital Expenditure	Revenue Expenditure
Structural maintenance of roads, bridges & footpaths.	Routine maintenance of roads, bridges & footpaths (e.g. filling potholes).
Extending a building.	Maintaining a building (re-pointing, repairing minor cracks, painting etc).
Structural repairs on a building, where the value has been written down in the accounts to reflect damage.	Repairs for damage not reflected by a reduction in the value of the building in the accounts.
Major refurbishments or overhauls that extend the life or value of an asset beyond its assessed standard.	Painting and decorating, routine maintenance.
Re-roofing of buildings.	Roof repairs or replacing broken tiles.
Upgrading poor quality old windows with new, higher quality ones.	Window repairs or replacement of broken windows.
Installation of central heating.	Replacement of central heating or broken parts of a heating system.
Improvement of floor structures.	Floor coverings.
Installation of new kitchens or toilet facilities.	Repairs or replacement of kitchen or toilet fittings.
Installation of water supply services/equipment.	Repairs or replacement of water supply services/equipment.
Installation of new systems and plant, where additional or more advanced and not a like-for-like replacement.	Like-for-like replacement of systems and plant within a building.
Removal of asbestos where a risk to health and safety and affecting the use or value of the building.	Removal of asbestos where it poses no risk to health or value of the building if left in situ. Inspection, air-testing and protective sealant treatment relating to asbestos.
Remodelling to make a building fit-for-purpose that it otherwise would not be.	Remodelling that does not significantly affect the service provided.
Legal & project management fees, architects', surveyors' and engineers' fees where directly attributable to an	Feasibility studies and finance fees.

**Examples of Capital and Revenue Expenditure
Detailed Examples**

Element	Capital	Revenue
Structural		
Roof	<p>New Structure</p> <p>Replacement of all or a substantial part of an existing structure to prevent major failure</p> <p>Screed/Insulation: New, replacement/repair of substantial part</p> <p>Edge/Finish/Trim/Fascia/Bargeboards on new build</p> <p>Drainage on new build</p>	<p>Repair/Replacement of small part of an existing structure</p> <p>Repair/Replacement of screed/insulation where defective</p> <p>Work to improve insulation standards</p> <p>Replacement of roof finish</p> <p>Repairs/replacement/Repainting</p> <p>Clearing gutters/downpipes</p> <p>Replacement/repair of individual gutters/pipes</p>
Floors	<p>Structure and Damp Proofing Course in new building.</p> <p>Replacement of all or a substantial part of an existing structure to prevent major failure.</p> <p>Screed and finish in new build.</p> <p>Replacement of all existing flooring</p>	<p>Repair and replacement of small parts of structure/DPC.</p> <p>Repair and replacement of some/part screed and flooring.</p> <p>Maintenance/Re-varnishing wooden floors</p>
Ceilings	<p>Suspension/membrane/fixed and access panels – new build</p> <p>Specialist removal/replacement of damaged/disturbed Asbestos based materials, planned or emergency</p>	<p>Suspension/membrane/fixed and access panels – repair or replacements including from water damage.</p> <p>Inspection/Air testing. Applying sealant coats to asbestos surface for protection.</p>
External Walls and Chimneys	<p>Structure Underpinning/propping for new build.</p> <p>External finish on new build</p> <p>External finish on existing builds where needed to prevent imminent or correct actual major failure of structure.</p>	<p>Repairs/Preventative measures i.e. tree works</p> <p>Repair/replacement of small parts of an existing structure e.g. re-pointing/re-cladding a proportion of a wall where failure has occurred.</p>
Internal Walls and Partitions	<p>Completion including various internal finishes, linings and decorations on new build or major refurbishment and alterations.</p>	<p>Repairs and decorations to internal plaster / linings etc.</p> <p>Minor alterations.</p>
Windows and Doors	<p>Framing on new build.</p> <p>Framing – structural replacement programme.</p> <p>Glazing on new build</p> <p>Glazing – upgrading all or substantial part of existing glazing</p>	<p>Repair and replacement of individual frames / windows. Repainting frames/windows.</p> <p>Replacing broken glass</p> <p>Repair/replacement or upgrading locks.</p> <p>Internal and external decoration.</p>

Sanitary		
Lavatories	Provision in new buildings of all toilet fittings, waste plumbing and internal drainage. Large scale toilet refurbishment Provision of disabled facilities and specialist facilities.	Repair or replacement of damaged sanitary ware, fittings, waste plumbing etc Small areas of refurbishment
Kitchens	Kitchens in new buildings complete with fittings, equipment, waste plumbing and internal drainage. Internal finishes and decorations.	Maintenance of kitchens. Cleaning out drainage systems Redecoration, general refurbishment and minor repairs.
Mechanical Services		
Heating and Hot Water systems	Complete heating and hot water systems to new projects including fuel storage, controls distributions and flues. Safe removal of old/damaged asbestos boilers and pipe work insulation where risk to H&S. Planned replacement of old boiler/controls systems past the end of their useful life. Emergency replacement of boiler plant/systems	General maintenance of all boiler house plant including replacement of defective parts including regular cleaning.
Cold Water	Provision of cold water services, storage tanks, distribution, boosters, hose reels etc. Major planned replacement of cold water services.	Maintenance and repair/replacement of defective parts such as servicing pipes. Annual servicing of cold water systems
Gas	Distribution systems on new and major refurbishments.	Repairs and maintenance and gas safety. All servicing.
Ventilation	Mechanical ventilation and air condition on new or major replacements.	Provision of local ventilation. Repair/replacement of defective systems and units.
Other mechanical services	Major plant (ie swimming pool, heat recovery systems) installation.	Repair/replacement of parts to plant, pumps and controls. Water treatment equipment repair/servicing.
Electrical Services		
General	Main switchgear and distribution in major projects. Replacement of obsolete and dangerous wiring systems, including distribution boards.	Testing/replacement of distribution boards. The repair and maintenance of all switchgear and interconnecting cables. All testing, earthing and bonding to meet H&S. All servicing
Power	Control gear, distribution, fixed equipment and protection on new build or major refurbishment.	All testing, repair and replacement of small items of equipment.

Lighting	Provision of luminaries and emergency lighting. Major replacement throughout building	Ad-hoc replacement of luminaries, all testing, adjustments and improvements.
Other Electrical Services	Lightning protection in new build. Provision of alarm systems, CCTV, lifts and hoists. New installation of communication systems, radio/TV, telephone, data transmission IT etc including provision in new build.	Repair, maintenance or minor replacement
External Works		
Pavings	Provision of new roads, car parks, paths, courts terraces, play pitches, steps and handrails as part of a major project, including disabled access.	Maintenance and repair – car parking and playground markings
Other	Provision of walls, fencing, gates and ancillary buildings as part of a major project.	Maintenance and repair of all perimeter/boundary retaining walls, fencing and gates.
Drainage	Drains, soakways, inspection chambers and sewage plant as part of major project.	Maintenance and repair of drains, gullies, grease traps and manholes. Cleaning of the above and unblocking as necessary.
Open air pools	Structural provision	Hygiene cleaning and maintenance and repairs.
Services distribution	Heating mains, gas mains, water mains, electricity mains and renewal of any above	Annual servicing.