Capital versus Revenue expenditure

1. **Definitions**

a) CAPITAL EXPENDITURE is money spent to buy fixed assets.

b) REVENUE EXPENDITURE is money spent on the daily running expenses of the business.

2. **Examples of differences between Capital and Revenue expenditure**

CAPITAL EXPENDITURE	REVENUE EXPENDITURE
Purchase a building	Rent a building
Buy a new vehicle	Repair a vehicle
Addition to a new building	Redecorating existing building
Installation cost of new equipment	Electricity costs of using the equipment

From the example, you should note that:

Any money spent when a fixed asset is ***FIRST*** purchased must be treated as Capital Expenditure eg Cost of a new computer; costs to transport the new computer; costs to install the new computer; costs to train employees to use the new computer.

Any expenditure on the fixed asset after it has been used for a while is treated as Revenue Expenditure eg repairs to the computer; electricity costs.

3. **Incorrect treatment of expenditure**

a) What is the effect if Capital expenditure is incorrectly recorded as Revenue expenditure?

Example: the purchase of Equipment is incorrectly recorded as Stationery

Answer: Net Profit be lower than it should be (understated)
The Equipment on the Balance Sheet would be lower than it should be (understated)

b) What is the effect if Revenue expenditure is incorrectly recorded as Capital expenditure?

Example: repairs to a vehicle is incorrectly recorded in the Vehicle account

Answer: Net Profit would be higher than it should be (overstated)
Vehicles on the Balance Sheet would be higher than it should be (overstated)