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I Know It When I See It – What is a Capital Expenditure? - Squire Patton Boggs

According to Wikipedia, the fount of all knowledge, the phrase "I know it when I see it" is a colloquial expression by which a speaker attempts to categorize an observable fact or event, although the category is subjective or lacks clearly defined parameters. This phrase was famously used in a U.S. Supreme Court decision to describe the threshold test for obscenity. (See *Jacobellis v. Ohio*, 378 U.S. 184 (1964)). Although this blog post will, unfortunately, likely not become as well known as the *Jacobellis* case, it will discuss, "What is a Capital Expenditure?" My guess is that a lot of tax-exempt bond advisors use intuition when determining that certain expenditures qualify as "capital expenditures" for tax-exempt bond purposes. In other words, they know a capital expenditure when they see one. However, the question as to what constitutes a "capital expenditure" under the tax-exempt bond rules may be difficult to answer at times.

Treas. Reg. Section 1.150-1(b) defines "capital expenditure" as:

> any cost of a type that is properly chargeable to capital account . . . under general Federal income tax principles. For example, costs incurred to acquire, construct, or improve land, buildings, and equipment generally are capital expenditures.

Without the example provided, I am not sure I would know what type of expenditure is "chargeable to capital account." Luckily, the example makes it clear that both the acquisition of a building and the construction of a building clearly qualify as capital expenditures. However, it becomes more difficult to determine whether an expenditure "improves" a building. For example, does a replacement of windows in a building "improve" a building or merely "maintain" the building under general Federal income tax principles? Does it matter if some of the old windows were cracked, or that the new windows are more energy efficient?

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By Cynthia Mog on January 23, 2023

The Public Finance Tax Blog

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