

Working in Practice

Use of Home Expense

Before working from home it will be necessary to check that there are no restrictions by covenant, or by the mortgagor, and that planning regulations are not being infringed.

An employer can reimburse an employee for use of home and the Inland Revenue would not consider £2.50 per week to be excessive. Higher payments would need to be justified. From February 2007 HMRC have issued clearer guidance and details of that are listed below. The full guidance can be found at

<http://www.hmrc.gov.uk/manuals/bimmanual/BIM47800.htm>

A Self-employed person working from home needs to consider various points before charging an expense of Use of Home to their business:

1. The amount of time actually spent working from home. A trade person would spend less time working at home than an accountant who may work full-time from home.
2. The amount of space devoted to business. Part of a room, one or more whole rooms or even an extension, and the percentage of business space to the whole house.
3. The possible impact of Capital Gains Tax upon the selling of the house.
4. The business use must be covered by the house policy or a separate business policy.

A proportion of household overheads can be claimed (lighting and heating, cleaning, renewal and maintenance costs of decorating and repair), but beware when considering rates or council tax because of the Capital Gains Tax when the house is sold.

The rule applies that the expense must be wholly, exclusively or necessary for the business.

If however Capital Gains Tax is levied, then it will only apply to the net gain on the sale of the property after allowance for index linking up to April 1998 and then taper relief to reduce the actual gain to business use. This is then offset against the annual Capital Gains Tax Relief. The balance of the gain is Tax Exempt as a domestic residence

What HMRC considers to be allowable depends on the facts in each case.

Expenses broadly fall into two categories, fixed costs and running costs.

Fixed costs relate to the whole house and have to be paid even if there is no business use. These include costs such as, Council Tax, mortgage interest, insurance, water rates, general repairs and rent.

If the business buys "use of home" insurance the business is covered by a separate policy and the cost of that policy is allowed in full, but no part of the household policy is allowed.

Otherwise, an appropriate part of the premium can be allowed

There will be council tax on the property. In principle it may be allowable in those instances where other property based expenses are deductible. If business use is established the appropriate proportion already applied may be allowed under the normal rules for the deduction of expenses.

If part of the home is used solely for business then an appropriate part of the mortgage interest is an allowable deduction. Repayments of capital are not allowable.

Part of the rent is an allowable expense when the home is rented and part is used solely for business purposes.

A sole trader cannot charge a separate rent to his or her own business.

A proportion of the cost of general household repairs and maintenance is allowable in line with the proportion that the house is used solely for the business. HMRC examples include the general redecoration of the exterior or repairs to the roof.

Repairs that relate solely to part of the house that is not used for the business, such as decorating a room not used for the business, are not allowable. Equally if a room is used solely for business purposes then the cost of redecorating that room is wholly allowable.

HMRC recognize that there are some expenses where the total bill may vary with the amount of business use. They include cleaning, heat and light and metered water.

If the claim is small and there is only minor business use of the home, for example the taxpayer writes up their business records at home, HMRC may accept a claim based on any reasonable basis.

Where there is significant business use it is appropriate to apportion such expenses by reference to the facts of that usage.

A proportion of the heating and lighting costs of a room used at times solely for business purposes are allowable. The proportion should reflect the facts of usage. The number and nature of any power consuming items involved should also be considered. HMRC give the example of a commercial photographer working from home using specialist studio lighting who will have a much higher business expense for electricity than a trader writing up records once a week in the spare bedroom.

The cost of business calls is allowable, including a proportion of the line rental (based on the ratio of business use to total use). This proportion should reflect all aspects of use, including incoming calls, though HMRC accept that in most cases reference to itemised outgoing calls will provide a reasonable and acceptable measure.

Care should be taken and a flexible approach adopted when considering the level of apportioned business expenditure, relating to all inclusive packages offered by telephone and broadband providers.

Expenditure on an internet connection (including broadband and wireless broadband) is allowable to the extent that the connection is used for business purposes. Where there is 'mixed' (business/non-business) use, follow the approach used for telephone rentals.

With water metering where there are cases of heavy usage the business part of the property may be separately charged (and so fully allowable) in which event none of the domestic cost is deductible.

In the case of minor business use of the premises, such as writing up records, there is no business use of water and so none of the water charge is allowable.

An example is the best way to illustrate this point.

Assume that one whole room is used for business use and represents one eighth of the house, and is used full time by the self-employed person working at home

| | |
|--|-------|
| Electric power and lighting – annual cost £ 350 | |
| Estimated 70% to business | £ 245 |
| Heating – annual cost £ 700 | |
| Estimated 70% to business | £ 490 |
| Cleaning and maintenance- annual cost £ 500 | |
| Estimated 12.5% to business | £ 63 |
| Replacement of carpets decorating etc – annual cost £500 | |
| Estimated 12.5% to business | £ 63 |
| Total annual cost to business | £ 861 |

The above is purely an example and must not be taken as approved by the Inland Revenue.

HMRC have published more examples which can be found at

<http://www.hmrc.gov.uk/manuals/bimmanual/BIM47825.htm>

There are situations where an employee may be field based and use their home as an office. The tax office must be contacted in these cases to confirm what expenses can be claimed for use of home. Any agreed expenses are then put into box 1.35 of the employment section of the self assessment return. Employees who work from home are entitled to a deduction under Section 336 ITEPA 2003 for a proportion of their household expense.

Section 336 provides relief for expenses that an employee is obliged to incur and pay **wholly, exclusively and necessarily** in the performance of the duties of the employment.

For an expense to be deductible under Section 336 it must be one that the employee is obliged to incur solely because they **are** employed, and not because of any reasons personal themselves. Any element of personal choice as to whether the employee works at home or at the employer's premises will prevent a deduction under Section 336 for those employees who choose to work from home.

The Employment Income Manual, at EIM32775, reduces the underlying law to two non-statutory tests. They are:

- that the duties that the employee performs at home are substantive duties of the employment; and
- that there is an objective requirement that those duties should be carried out at the employee's home **and nowhere else**.

The National Child Minders Association (NCMA) has some very useful guidelines that have been agreed with HMRC where a childminder operates a business from within their own home.

The agreement allows for expenses that include a percentage of certain household costs and relate to the number of hours the childminder works per week. The hours do not exceed 40 hours per week as this is the maximum that can be claimed.

Bills are required to be kept as part of the accounts.

Allowable expenses (NCMA)

| Hours Worked | Heat and Light | Water Rates | Council Tax | Wear and Tear |
|--------------|----------------|-------------|-------------|---------------|
| 10 | 8% | 2% | 2% | 10% |
| 15 | 12% | 4% | 4% | 10% |
| 20 | 17% | 5% | 5% | 10% |
| 25 | 21% | 6% | 6% | 10% |
| 30 | 25% | 7% | 7% | 10% |
| 35 | 29% | 9% | 9% | 10% |
| 40 | 33% | 10% | 10% | 10% |

These figures have been agreed by the NCMA and HMRC and should be used as a guide only. Childminders work almost exclusively from home, and if self employment takes someone away from the home for prolonged periods of time, these figures would have to be adjusted to reflect that.

HMRC have issued new guidance notes on use of home and we will be updating our notes as soon as we have assessed the impact to Accountants working in practice.