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**When your home is also  
your place of business**

## There can be tax implications if you trade from home, or use your home as your office. What about tax relief for household costs? Capital gains tax? Business rates? We look at these and other issues here.

### Why your employment status matters

If your home is also where you trade or work, your tax position hinges on one critical distinction.

That's whether you are self-employed or an employee. The tax treatment of partners and sole traders is different from the tax treatment of employees: broadly speaking, the regime is more favourable to the self-employed than employees.

It should be remembered, too, that the rules for employees apply to company directors, who are technically officers of their limited company, and to other company officers. It doesn't just apply to those who automatically identify as employees, such as those with long-standing homeworking arrangements in place, or those starting to work from home during the pandemic.

**Tip.** If you are self-employed and carry on most of your trade outside the home, you may still get a deduction for some household expenses, provided there are times when part of your home is used solely for business purposes. If there's only minor use of the home – perhaps you simply write up business records at home and trade elsewhere, HMRC should accept a reasonable estimate of costs without detailed enquiry.

### Expenditure, tax relief and the self-employed

To be allowable for tax purposes, costs must be incurred wholly and exclusively for the purposes of the trade. Such costs may include fixed costs like insurance, council tax, mortgage interest and rent. What's allowable will depend on the exact circumstances of your business: how much of your business you carry out at home, and indeed, what sort of business it is.

**Tip.** If the home is rented and part of it is used solely for business purposes, part of the rent is an allowable expense. Note, however, that while

sole traders cannot charge a separate rent to their business, the position is different for partners and company directors (see below).

Running costs, such as cleaning, heat and light and power and metered water, also attract relief. Relief can also be given for costs that might include a private element, so long as it's possible to identify a definite part of the expense as being wholly and exclusively for the purposes of the trade. This may include the cost of business calls on the home telephone and a proportion of the line rental, and expenditure on internet connections, to the extent that the connection is used for business. Any part of the cost not directly attributable to the business is disallowed. So, for example, 10% of a utility bill might relate directly to business use: the remaining 90% would be disallowed.

**Tip.** To qualify under the wholly and exclusively rule, you don't need to have the business element billed separately: nor to set part of the house aside for business use and nothing else.

In practice, tax relief is given in one of two ways. Either part of the cost is apportioned to the business, as in the 10%:90% example above, and receives tax relief; or there is an option to use fixed-rate deductions. Generally, using fixed-rate deductions means slightly less generous relief, but also less by way of administration.

### Apportioning expenses

To arrive at a reasonable apportionment, the type of factors to consider are:

- area: what proportion in terms of area of the home is used for trade purposes?
- usage: how much is consumed? This is appropriate where there is a metered or measurable supply, such as electricity, gas or water.
- time: how long is it used for trade purposes, and how does this compare with any other use?

Where a nominal sum of only a few pounds per week is claimed, HMRC is likely to accept a reasonable estimate. In other cases, it will be appropriate to keep records to substantiate claims.

### Example

Catriona is an online tutor, who works from home, primarily in the living room. The room is used eight hours a day: Catriona uses it for work for four hours in the morning, and at night the family uses it for four hours. In terms of size, the room represents 10% of the area of the house. In terms of time, its use is half business, half private.

Electricity for the year totals £1,500. This includes the cost of heating and lighting the room and powering Catriona's work computer. Electricity costs are apportioned by area and time. 10% of the costs (representing 10% of the area used) = £150. Half of this (representing 50% of the time used) = £75.

Catriona keeps a work diary to substantiate her hours of work, as well as invoices for the costs incurred.

### Fixed-rate deductions

The alternative to apportioning household expenses is to use fixed flat rate deductions. These apply to certain household running costs, and are based on the number of hours spent wholly and exclusively on core business activities. They are only available if hours total 25 or more per month. Core business activities are defined as providing goods and/or services, maintaining business records, and marketing and obtaining new business. The flat rates are:

Hours worked	Flat rate monthly deduction
25 or more	£10
51 or more	£18
101 or more	£26

Using fixed-rate deductions doesn't rule out a separate deduction for certain other fixed costs, such as council tax and mortgage interest, where an identifiable proportion can be attributed to

business use. You may also be able to claim a deduction for telephone and broadband/internet connection costs, and we should be pleased to advise further.

### Capital expenditure

For the self-employed, tax reliefs known as capital allowances cover the depreciation of capital assets. Capital allowances may be available on the business proportion of assets like laptops, printers, desks, chairs, filing cabinets and other office equipment. Adjustments are made for any non-business use.

### Travel costs

Where there are no business premises other than the home, it may be possible to claim travel costs to visit clients. But where there is more than one place of business, of which one is a home office, HMRC may maintain that travel between them does not comply with the wholly and exclusively test. Travel costs can be contentious, and we should be pleased to provide in-depth advice here.

### Capital gains tax

It's often asked whether using the home for business purposes has capital gains tax (CGT) consequences. In fact, business use is unlikely to do so, unless part of the home is used exclusively for business.

It is always prudent to take care in this area. The CGT exemption known as private residence relief (PRR) applies only to the residential part of a house. This means that where there is exclusive business use of one part of the house, PRR could be restricted, though other tax reliefs may be available.

### Example: drawing the boundary

Henryk and Lois are selling their small guest house and their accountant is advising on possible capital gains. The rooms used as guest bedrooms represent exclusive business use, but the kitchen, used both to cook their meals and guests' meals, does not.

By contrast, Dr Munro uses a room in his home as a surgery. Although it houses a cupboard in which he keeps a collection of maps and some climbing

equipment, HMRC is likely to consider that this room is used exclusively for business.

## Business rates

Many home-based businesses aren't liable for business rates, if only a small part of the home is used for business. But liability can arise in some cases, for example if a room is used exclusively for business, or if property is structurally modified for the purposes of the business.

## What about employees?

Employers can normally provide equipment to enable employees to work from home, but costs paid by an employer on an employee's behalf, are generally taxable. So too are reimbursed costs. The employee would need to claim any tax relief available personally.

For employees, the golden rule for tax relief is being able to show that an expense is incurred wholly, exclusively and necessarily in the performance of the employee's duties. The requirement to demonstrate something is 'necessary' makes it more demanding than the wholly and exclusively test for the self-employed.

A specific exemption can be used to allow employers to contribute – without a tax liability - to reasonable additional household costs incurred by employees working at home. These might be additional costs of heat and light for the work area, or the metered cost of increased water use. A flat rate of £6 per week, or £26 per month for monthly paid employees, can be paid without any need for employees to record expenditure. Employers can pay more than this, though the record keeping requirement increases correspondingly.

The exemption applies where a homeworking arrangement is in place. Two tests have to be met here. Specific arrangements between employer and employee must have been made. These will usually (though not necessarily) be set out in writing. And the employee must work at home regularly under these arrangements.

## Covid-19 rules

There's a temporary exemption from 16 March 2020 to 5 April 2022 to support employees working from home during the pandemic and buying home office equipment. It applies where employers reimburse the cost of equipment like a chair or monitor. As outlined above, this would normally be taxable, but where the following conditions are met, there is a temporary exemption from income tax and national insurance:

- equipment is obtained solely to enable an employee to work from home because of the pandemic
- it would have been exempt from income tax if provided directly to the employee, either by the employer or on their behalf
- such arrangements are available to all other employees of the business generally on similar terms.

Current and future ownership of such equipment may have tax implications and we can advise further here.

## Tip for directors and partners

It will usually be beneficial for directors and partners who work from home to put in place a formal rental agreement between themselves and the company/partnership. Rent paid at a commercial rate would constitute an allowable deduction for the company/partnership.

Advice is needed to get such agreements right, guarding against HMRC challenge and possible loss of PRR further down the line. There are also tax implications for the individual director/partner concerned and we should be delighted to explore the issue with you in more depth.

## Working with you

We have only been able to give an overview of the rules in this Briefing. Please contact us for further information or advice: we are always available to help.