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Guide to Self-Employed Expenses

Whether you're a plumber, a mobile hairdresser or a physiotherapist you'll incur costs as a result of running your business.

We've put together a quick summary of the expenses that you may be able claim. These notes reflect the position at the time of writing (May 2012,) however you should be aware that they are a 'simplified' version of HMRC's vast guidance. Further information is available from HMRC or Taxback.com's UK tax technicians.

Basically your 'profits' are your income less expenses, and you only get taxed on your profits, so the higher your expenses, the lower your tax bill. If your earnings are £10,000 a month and you have £2,000 of expenses, you would only pay tax on the £8,000 (if you aren't VAT registered, the total amount spent on the expenses, including VAT, is deductible).

Buying or improving capital items, such as a van, machinery, business premises, a computer, fixtures and furniture which last for several years etc… are not business 'expenses' for tax purposes but you may still be able to claim relief for them as long as they are related to your business. Capital items need to be shown separately on your Self Assessment tax return, but will also reduce your taxable profits.

Any expenses must be applicable to the running of your business. You can't take away any private expenses. The general rule is that a self employed person cannot deduct expenses unless they are 'wholly and exclusively' laid out for the purposes of the trade, profession or vocation.

It's worth bearing this in mind, because you may be asked to provide evidence by HMRC that firstly, you actually incurred an expense and secondly, the expense was wholly and exclusively for your business. There is no point making them up just so you can pay less tax - penalties are severe. There is a guide to record keeping here:

Record keeping at a glance

Keeping up-to-date and accurate records from the start is important for your business. It makes it easier to complete your tax return. A good record system helps you keep track of your expenses. If you do not keep adequate records or complete your tax return correctly or on time you may have to pay a penalty.

What records to keep	Anything to do with your business such as: • cashbooks • invoices • mileage records • bank statements • receipts for purchases • CIS vouchers

How to keep your records	Either on paper or on computer. For electronic records you must: • capture all the information (front and back) • save information in a readable format • keep a back-up
How long to keep records	As a general rule for a minimum of six years.

Allowable expenses

In most cases it will be clear if something has been incurred *wholly and exclusively* for the purposes of business - provided a receipt has been kept as proof of purchase, a deduction should be allowed. A table of the most common allowable (and disallowable expenditure) is included at the end of this section.

However, a newly established business is often run from home, perhaps using an existing car for any business travelling that is required and an existing mobile phone for business calls. This can cause problems, because of the 'duality' of purpose, inherent in many such costs. It is therefore necessary that you can clearly identify and separate the expenditure between business and private purposes.

Here we look at these particular elements in detail – you should be aware that such claims are under HMRC scrutiny at the moment so it is important that you understand the rules.

Motoring expenses

If you use a car both for business and privately, you can claim a proportion of the actual running costs e.g. fuel, oil, servicing, repairs, insurance, vehicle excise duty and MOT etc – usually in the ratio of your *business mileage* to your total mileage.

You must keep a log of business mileage as well as copies of all bills/receipts to calculate the appropriate deduction. The concept of *business* mileage is explored later on.

You can alternatively use a fixed rate per business mile to compute vehicle expenses instead of keeping detailed records of actual expenditure. This method is intended to make things simpler for small businesses. It is available if the annual turnover of a business is less than the VAT registration threshold when they first use the vehicle (GBP77,000 in 2012/13). The amounts to use are:

• car or van 45 pence a mile for the first 10,000 miles and 25 pence a mile thereafter
• motorcycle 24 pence a mile
• cycle 20 pence a mile.

Taxpayers can only use the mileage rate basis if they apply it consistently from year to year. They can only change to or from an 'actual' basis when a vehicle is replaced. The mileage rate covers the costs of running and maintaining the vehicle, such as fuel, oil, servicing, repairs, insurance, vehicle excise duty and MOT. The rate also covers depreciation of the vehicle. So if a taxpayer uses the mileage rate basis then they cannot claim any additional amounts for these expenses.

Any deductible journeys must have been made *wholly and exclusively* for business purposes and a log of business mileage should be kept. Whatever your business and however you work out your motoring expenses, you must keep adequate records to back up your tax return. Please note that costs of motoring for mixed private and business purpose is non-allowable expenditure. An example would be the cost of travelling to town to bank the business takings and do your private shopping at the same time.

What constitutes business miles?

Where a taxpayer owns or rents separate business premises away from their residence then the general treatment is as follows: The cost of travel between the taxpayer's home and the work base is not allowable (this is ordinary commuting) The cost of travel between the work base and other places where work is carried out, is an allowable expense.

There are some types of business where the taxpayer has no separate business premises away from home. For example an insurance salesman who has no office away from his residence, but who visits clients.

Provided their base of operations is at their home, the costs of travelling between the residence and the sites at which they work may be allowed. This is because they travel from their home to a number of different locations for a purely temporary purpose at each such place – to complete a job of work. At the conclusion of which, they will attend at a different location.

In such cases, taxpayers would normally visit a large number of different premises to carry on business.

The position is rather different where a trader works at one or two different sites only during the year – for example a construction subcontractor working on the Olympic stadium. This is the normal pattern of his business, so the one or two sites will be the normal working place for the subcontractor. As such, the cost of travelling between the subcontractor's home and such business 'bases' should be disallowed because it is just ordinary commuting.

Where the subcontractor travels regularly at their own expense to a work base to receive instructions from a 'principal' and then is conveyed (at the principal's expense) to another location/s, the subcontractor will have no allowable travel costs.

Example

Dave is a subcontracted solar panel fitter. His work base is five miles from his home and it costs him £2 a day in petrol to get there and back. He goes there first thing everyday to get changed into his special work clothes, meet his work mate, take instructions form his principal as to the installation job for the day and pick up the work van and tools. He is given a fuel card by the business to charge petrol too and on average £40 a day is spent. At the end of the working day, Dave will return the work van to the depot and from there, go home in his own vehicle. There are no allowable business travel expenses.

If he, instead, funds the costs of such travel and between the work base and other work locations himself (i.e. if he had to use his own van and pay £40 petrol a day) a deduction may be permitted for this business travel.

It is sometimes possible where a subcontractor's home is their business base (the taxpayer may at times work there, keep their business records, materials, tools there etc) and works at many different sites during a year that they can be called a 'itinerant' trader. Travelling expenses between the taxpayer's home and those sites should normally be allowed.

Example

Paul is subcontracted granite fitter. His contractor has a depot 25 miles away from his home where sheets of granite are kept, ready to be cut up into kitchen worktops. He drives there once or twice a week in his van to pick up granite and get his forthcoming job sheets. For the rest of the time he is based at 'home' – keeping his tools there, writing his records up, making template drawing of jobs, communicating with his contractor and customers to arrange work and provide updates. He makes five or ten customer visits a week to measure or fit jobs. Mostly these are directly from home. Sometimes these are from his contractor's base. Paul is an 'itinerant' trader - all of his travel expenses should be deductible.

Use of home as office

Where a room at home is used wholly and exclusively for business purposes, a deduction may be claimed for the additional costs of the business use, such as light and heat.

Wholly and exclusively means that when part of the home is being used for the business, then that is the *sole use* for that part at *that time*. Thus, if the part of the home used for business purposes, e.g. drawing up invoices is also, at the same time, used for some other non-business purpose, e.g. watching television, then no deduction is due.

The question is therefore whether there are periods when part of the home is being used solely for business purposes. If part of the self-employed person's home is set aside solely for business use for a period, they can claim as a deduction the costs they incurred on that part during that period. It will be most unlikely that they have a separate bill for that specific part and usually this exercise will involve apportioning the total relevant bill between the period of solely business use and the remainder of the time covered by the expense.

In the right circumstances, it is possible to claim a portion of: insurance council tax, mortgage interest, rent, repairs and maintainence, cleaning, heat, light and power, broadband and telephone – including a portion of line rental.

The factors to be taken into account when apportioning an expense include:

- Area: what proportion in terms of area of the home is used for business 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 business purposes, as compared to any other use?

The method of apportioning an expense depends on the relative importance of each of these factors.

Example

Chris is an author working from home. She uses her living room from 8am to 12am. During the evening, from 6pm until 10pm it is used by her family. The room used represents 10% of the area of the house.

The fixed costs including cleaning, insurance, Council Tax and mortgage interest, etc total £6600. A tenth of the fixed establishment costs is £660 (representing the room). One sixth (4/24) of the use, by time, is for business, so Chris claims £110.

She uses electricity for heating, lighting and to power her computer, which costs £1500 per annum. Chris considers an apportionment of these costs by time and area. A tenth of the costs are £150 and half of these costs by time (4/8) relate to business use, she claims £75.

She also uses the telephone to connect to the internet for research purposes. Her itemised telephone bill shows that a third of the calls made are business calls. She can claim the cost of those calls plus a third of the standing charge.

Administrative costs, including mobile phone

You can deduct the administrative costs of running your business, including advertising, stationery, postage, telephone and fax. You may also be able to deduct the cost of trade or professional journals or subscriptions.

With regards to mobile phones, the simplest way of demonstrating that mobile phone costs are wholly and exclusively for the purposes of trade is to keep a separate contract phone for business and retain your phone bills as evidence that you have two phones – one for business, one for personal.

Any claims for significant business mobile phone use of on an otherwise personal mobile phone, are likely to be queried and tested, so again, bills should be kept to demonstrate the personal v work usage.

Disallowed expenses

Please note that some expenses are never allowable for tax purposes, for example, entertaining clients, even if such entertainment directly led to new business.

And, private expenditure - private expenditure is non-allowable expenditure - you can't get tax relief for it. Here are some examples:

- Ordinary 'civilian' clothing.

Expenditure on ordinary clothing worn during the course of a trade is disallowable. This remains so even where particular standards of dress are required by, for example, the rules of a professional body.

The cost of clothing that is not part of an 'everyday' wardrobe faces no such bar to deduction. A deduction for protective clothing and uniforms is therefore normally allowed.

- Food for sustenance.

The cost of food and drink is not in general an expense incurred wholly and exclusively for business purposes, since everyone must eat in order to live. They are normal costs of living incurred by all and not as a result of trading.

It is immaterial that the physical demands of the taxpayer's occupation require a greater consumption of food or that the location of the work place imposes a greater cost.

Where occasional business journeys outside the normal pattern are made, so that extra costs are incurred in having to lunch away from home or the normal work base for example, modest expenses incurred in these circumstances may be deducted from business profits.

- Having somewhere to live.

The cost of domestic living accommodation is not allowable, notwithstanding that the expenditure allows the taxpayer to do more work.

For example, Andrew is a self employed CIS contractor living in Coventry. He claims the costs of weekly travelling to and from, and living during the week in Kent (200 miles away) where he has been working on a contract for at seven years. All deductions are likely to be denied. The choice of where you live is a personal choice.

Where a business trip necessitates one or more nights away from home, the hotel accommodation and reasonable costs of overnight subsistence may be deductible.

Expenses summary

Category	Allowable expenses	Non allowable expenses
Accountancy, legal and other professional fees	Accountants, solicitors, surveyors, architects and other professional indemnity insurance premiums.	Legal costs of buying property and large items of equipment; costs of settling tax disputes and fines for breaking the law.
Advertising and business entertainment costs.	Advertising in newspapers, directories etc. mail shots, free samples, website costs.	Entertaining clients, suppliers and customers; hospitality at events.
Bank, credit card and other financial charges.	Bank, overdraft and credit card charges; hire purchase interest and leasing payments. Alternative finance payments.	Repayment of the loans or overdrafts or finance arrangements.
Car, van and travel expenses.	Car and van insurance, repairs, servicing, fuel, parking, hire charges, vehicle licence fees, AA/RAC membership; train, bus, air and taxi fares; hotel room costs and meals on overnight business trips.	Non business motoring costs (private use proportions); fines; costs of buying vehicles; travel costs between home and business; other meals.
Communications, stationery and other office costs (mobile, internet, email costs).	Phone, mobile, internet, email and fax running costs; postage, stationery, printing and small office equipment costs; computer software	Non business or private use proportion of expenses; new phone, fax, computer hardware or other equipment costs.
Construction industry – payments to subcontractors.	Construction industry subcontractors payments (before taking off any tax).	Payments for non business work
Cost of goods that you are going to sell or use in providing a service.	Cost of goods bought for resale, cost of raw materials used, direct cost of producing goods	Cost of goods or materials bought for private use; depreciation of equipment.
Depreciation and loss/profit on sale of assets.	Depreciation and loss/profit on sale of assets are not allowable expenses – any amount entered here should also be shown in box 43 of the tax return.	Depreciation of equipment, cars etc. Losses on sales of assets (minus any profits on sales).
Insurance policy.	Costs of any business specific policy.	Recoverable costs
Interest on bank and other business loans.	Interest on bank and other business loans. Alternative finance payments.	Repayment of the loans or overdrafts, or finance arrangements
Irrecoverable debts written off.	Amounts included in turnover but unpaid and written off because they will not be recovered.	Debts not included in turnover; debts relating to fixed assets; general bad debts.
Other business expenses.	Trade or professional journals and subscriptions; other sundry business running expenses not included elsewhere.	Payments to clubs, charities, political parties etc.; non business part of any expenses; cost of ordinary clothing.
Rent, rates, power and	Rent for business premises,	Costs of any non business

insurance costs.	business and water rates, light, heat, power, property insurance, security; use of home as office (business proportion only).	part of premises; costs of buying business premises.
Repairs and renewals for property and equipment.	Repairs and maintenance of business premises and equipment; renewals of small tools and items of equipment.	Repairs of non business parts of premises or equipment; costs of improving or altering premises and equipment.
Wages, salaries and other staff costs.	Salaries, wages, bonuses, pensions, benefits for staff or employees; agency fees, subcontract labour costs; employers' NICs etc.	Own wages and drawings, pension payments or NICs; payments for non business work.