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Making money from your spare room

Under the rent-a-room scheme, it is possible to earn tax-free income from letting out a furnished room in your own home to a lodger. You can even use the scheme if you run a bed-and-breakfast or a guest house.

Rent-a-room is not available if the room is unfurnished, or if you let accommodation in a UK home while living abroad. The Government also intends to amend the rules so the scheme is not available to those who let accommodation via Airbnb and similar sites.

Automatic exemption

No tax is payable if the gross receipts from letting are less than the rent-a-room threshold, set at £7,500 a year from 6 April 2016. The exemption is automatic and does not need to be claimed. Even better, there is no need to tell HMRC about the income.

Gross receipts include rental income before expenses, any amounts received in respect of the provision of services, such as cleaning, meals or laundry, and any balancing charges.

Gross receipts exceed £7,500

If your gross receipts from letting a furnished room in your home exceed the rent-a-room threshold of £7,500, you can still benefit from the scheme. However, whether it is beneficial to do so will depend on the level of the associated expenses.

Where receipts exceed £7,500, you have a choice as to how to work out the rental profit on which you pay tax. Under method A, you simply deduct the associated expenses and any capital allowances and pay tax on the actual profit. Under method B, you deduct the rent-a-room threshold and pay tax on the difference.

So, if expenses are less than the rent-a-room threshold, method B is beneficial, whereas if they exceed the threshold, method A is better.

Example

In 2016/17, Greg lets out two furnished rooms in his own home to lodgers. He receives rental income of £8,000. His associated expenses are £1,000. Under method A, he would pay tax on the actual profit of £7,000 (£8,000 - £1,000). Under method B, he would only pay tax on £500 (£8,000 - £7,500).

The rent-a-room scheme is beneficial. Greg opts into the scheme on his tax return and claims the allowance.

Losses

Rent-a-room will not be beneficial if you make a loss, even if your rental receipts are below the rent-a-room threshold. Under the rent-a-room scheme, you cannot create a loss. Losses can be carried forward and set against future rental income.

More than one landlord

If a house is owned jointly by two or more people, the rent-a-room limit is halved so each person has a tax-free allowance of £3,750. This is the case regardless of the number of people receiving rental income from letting rooms in the property – so tax-free rental income per property cannot exceed £7,500.

Opt in and out

You can choose each year whether it is beneficial to use the scheme and opt in and out on your tax return by the normal filing date of 31 January after the end of the tax year.

Partner note: ITTOIA 2003, Pt. 7. Ch. 1 (ss 784 – 802); HMRC Helpsheet 223.

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