# CHAPTER 17

# LIVING ACCOMMODATION – TAXABLE BENEFITS

## 17.1 Introduction

If a house, flat or any property that is owned or rented by the employer is made available for use by an employee, there will be a taxable benefit for the employee as he is occupying a property provided to him by his employer.

The provision of **living accommodation is a taxable benefit for all employees** even lower paid employees.

The way that the benefit is taxed depends on whether the accommodation is "job related" or "non job related".

## 17.2 "Job related" accommodation

ITEPA 2003, s.99

If an employer provides an employee with job related accommodation, there is no benefit arising to the employee on the use of that accommodation.

**Job related accommodation** is accommodation which is **"necessary"** for the proper performance of the job. Employees such as **caretakers** on call outside normal working hours and lock-keepers will live in job related accommodation. In other words, where the employee can demonstrate that the occupation of the property is **essential** for the proper performance of the duties. Typically these are employees who are normally required by their employers to live on site in order to do their job.

Job related accommodation also covers situations where accommodation is provided, for the **"better performance"** of the employee's duties and it is **customary** for employers to provide living accommodation to such employees. For example it is customary to provide a **vicar** with a vicarage in the parish. This would constitute job related accommodation. Another example would be the manager of a public house living on the premises.

A director of a company cannot have his living accommodation classified as "job related" under s.99 unless either:

a) he does not have a "material interest" in the company (>5% of the shares); and either

b) he is employed as a full time working director, or the company is non-profit making or is established for charitable purposes.

Finally, if accommodation is provided by the employer because there is a threat to the employee's physical **"security"**, this will also constitute job related accommodation. Certain politicians such as the Chancellor or the Prime Minister live in job related accommodation on Downing Street and do not pay tax on the provision by the government of their living accommodation.

ITEPA 2003, s.100

## 17.3 Rented accommodation

For the rest of this chapter we are going to look at how we calculate the benefits where the accommodation provided to the employee is not job related. We will start by looking at how we calculate the cash equivalent where the **property is rented by the employer**.

The benefit - i.e. the cash equivalent - is **the higher of the rents paid by the employer** for the use of the property, **and the annual value of the property**.

ITEPA 2003, s.105(4)

The "annual value" of living accommodation is defined as the **rent** which might **reasonably be expected to be obtained on letting the property** if the tenant paid all the usual household bills and the landlord met all repair and maintenance costs. The "annual value" will be provided for you in the examination. As with most benefits this amount will be reduced where the accommodation is not available for the whole year.

ITEPA 2003, s. 110

In practice, HMRC will often use the **gross rateable value** of the property under the old rating system as the annual value. This will be much lower than the annual value as defined in the Act. If the property has no rateable value (for example because it was built recently), an estimate must be made. Any disputes as to the amount of the annual value will be dealt with by the first-tier tribunal.

We then deduct any **employee contributions** – i.e. any rents paid by the employee to the employer for the use of the property. This will give us the cash equivalent.

| | |
|---|---|
| Higher of: | |
| Rents paid by employer } | X |
| Annual value of property } | |
| Less: employee contributions | (X) |
| Taxable benefit | X |

Remember that this method of calculating the benefit only applies where the employer is **renting** the accommodation from another landlord.

It follows that if the employer only paid a small amount of rent in order to obtain the use of a property, the employee would only be taxed on a relatively small amount. Employers have entered into arrangements to take advantage of this by paying an upfront amount described as a lease premium, and thereafter only payment a very small rent.

Finance Act 2009 introduced legislation to counter such arrangements. For leases entered into on or after 22 April 2009 where a lease premium is paid for a lease of 10 years or less the amount of the premium will be treated as rent paid by the employer. In any tax year, the annual rent paid by the employer will be calculated as

ITEPA 2003, s.105A

$$\frac{\text{Lease premium}}{\text{Length of lease}} + \text{actual rent paid}$$

**Illustration 1**

Duncan is provided with a flat by his employer on 1 June 2010 (not job related accommodation). His employer leased the property for a period of 8 years commencing 1 June 2010. The employer paid a premium of £40,000 and pays rent of £100 per month. The annual value of the property is £1,000.

The taxable benefit for 2010/11 will be calculated as follows:

Higher of:

- Rent paid by employer

$$\frac{40000}{8} \times \frac{10}{12} = 4{,}167 + (10 \times 100) = £5{,}167$$

Note the accommodation is only available to Duncan for 10 months therefore only 10 months of rent is potentially assessable.

- Annual value

$$£1{,}000 \times \frac{10}{12} = £833$$

Therefore Duncan will be assessed on £5,167 in 2010/11.

## 17.4 Employer owned accommodation

**There are similar rules** where the **employer owns the accommodation** being made available to the employee.

Again, the starting point in calculating the benefit is the annual value. If the **accommodation cost the employer not more than £75,000,** then the benefit is equal to the annual value.

ITEPA 2003, s. 105(2)

If the house cost the employer **more than £75,000**, there will be an additional benefit to the employee called the additional yearly rent – this **extra benefit** will be **added to the annual value** to give the total benefit.

ITEPA 2003, s. 106

To calculate the additional yearly rent we start by taking the cost of the accommodation - "cost" means the original cost plus any improvements. From this we **deduct £75,000,** and **multiply** the difference by the **"ORI"** which is HMRC's official interest rate at the **start of the tax year**.

When calculating the "cost" of the property, only improvements carried out before the beginning of the tax year are taken into account. Improvements undertaken during the year will affect the "cost" used in calculating the benefit for the following year.

ITEPA 2003, s. 104

If the employee makes a contribution towards the benefit, this can be deducted in arriving at the taxable cash equivalent.

If employee contributions exceed the amount of the benefit, no loss will arise. The result is simply a benefit of zero.

| | |
|---|---|
| Annual Value | X |
| Add: | |
| Additional yearly rent if Cost > £75,000 | |
| £(Cost – £75,000) x ORI at start of year | X |
| | X |
| Less: employee contributions | (X) |
| Taxable Benefit | X |

**Illustration 2**

An employee lives in accommodation that is owned by his employer. The house cost the employer £160,000 and has an annual value of £1,000. The employee pays rent to the employer of £100 per month for the use of the house. Assume the official rate of interest is 4%.

The taxable benefit that will be entered onto the employee's form P11D will be as follows:

| | £ |
|---|---|
| Annual Value | 1,000 |
| Additional yearly rent: | |
| (160,000 – 75,000) x 4% | 3,400 |
| | 4,400 |
| Less: employee contributions: | |
| (£100 x 12) | (1,200) |
| Taxable Benefit | **£3,200** |

## 17.5 The "6 year" rule

ITEPA 2003, s. 107

The "6 year rule" applies when a house was bought by an employer and is made available for use by the employee **more than 6 years after it had been first acquired**. The additional yearly rental in respect of accommodation will not be based on cost. Instead, the charge will be based on the market value of the house on the date the property was made available to the employee.

In effect we are substituting market value in place of original cost. Note that this rule only applies where there are more than 6 years between the property being acquired by the employer and it being made available to the employee.

**Illustration 3**

An employee was provided with a house by his employer in June 1998. He pays £100 a month for use of the house. The house had been purchased for £100,000 in 1990 and has an annual value of £1,000. The house had a market value of £120,000 in June 1998. Assume an official rate of interest of 4%.

The benefit will be calculated as follows:

| | £ |
|---|---|
| Annual Value | 1,000 |
| Additional yearly rent £(120,000 – 75,000) @ 4% | 1,800 |
| Less: employee contributions | (1,200) |
| Taxable Benefit | **£1,600** |

As house prices normally rise over time, we would expect the original cost to be **less** than a later market value. However, if property prices fall such that when the employee moves in more than 6 years later, the market value is less than original cost, **this market value of the property will still be used to calculate the benefit** even though it is less than original cost.

If the original cost of the accommodation is **not more than £75,000**, there will **not be additional yearly rent**, regardless of current market value. For example, if a company buys a house in London in the 1960s for, let's say, £20,000, and the employee is given use of the property today when the house is worth, say, one million pounds, there is no additional charge because the original cost is below the £75,000 threshold.

ITEPA 2003, s. 107(1)(b)

If the **house is not made available** to the employee **for the whole of the tax year** - i.e. the employee moves in or moves out during the year - the benefit needs to be apportioned. Apportionment can be done on a monthly basis.

If the same living accommodation is provided for more than one employee at the same time, the cash equivalent of the benefit (as calculated above) is apportioned between the employees on a "just and reasonable" basis.

ITEPA 2003, s. 108

## 17.6 Household expenses

If the **employer pays** any household bills on behalf of the employee, for example **gas, electricity** and **telephone bills** etc, this will give rise to an additional and **separate benefit**. This benefit is calculated by taking the cost to the employer of paying these particular bills.

There is a special rule relating to expenses paid on behalf of employees who live in **job related accommodation**.

**Illustration 4**

Assume a vicar is living in job related accommodation. The vicar will not have a benefit on the provision of the house, as the accommodation is job related.

The vicar has a salary of £20,000 and his employer pays for the gas, electricity and telephone bills relating to the house. These come to £2,300. As the employer discharges these bills, this gives rise to an additional benefit.

The special rule says that where such expenses are paid on behalf of employees in job related accommodation, the amount on which the employee will be taxed in respect of this **benefit cannot exceed 10% of his other earnings from that employment for the year.**

ITEPA 2003, s. 315(3) & (4)

Here the vicar's earnings for the year is his salary of £20,000, so the amount on which the vicar will be taxed in respect of these reimbursed expenses cannot exceed 10% of this - ie £2,000.

This 10% restriction rule only applies to expenses provided for employees in job related accommodation. **Where the accommodation is not job related, the full amount of the expenses are taxable.**

In addition, where council tax or water rates are paid by the employer in respect of job related accommodation, the amount of the payments are exempt from income tax.

ITEPA 2003, s. 314

**Example 1**

Neil has lived for several years in a company owned flat. The flat cost the company £150,000 in 2002. The annual value is £800 and Neil pays rent of £150 per month. Neil moved out of the flat on 1 January 2011 and bought his own house.

**Calculate Neil's taxable benefit assuming that the official interest rate is 4%.**

**Example 2**

Alf is the manager of the Golden Lion Public House. He is employed on a salary of £18,000 and is required to live in the flat above the pub. His benefits for the year are as follows:

| | £ |
|---|---|
| Private medical insurance | 500 |
| Gas and electricity bills for flat | 2,200 |

**Calculate Alf's taxable employment income for the year.**

**Answer 1**

| | £ |
|---|---|
| Annual value | 800 |
| Additional yearly rent: | |
| £(150,000 – 75,000) @ 4% | 3,000 |
| | 3,800 |
| $\times \frac{9}{12}$ (6.4.10 - 1.1.11) | 2,850 |
| Less: employee contributions (£150 x 9) | (1,350) |
| Taxable Benefit | **£1,500** |

**Answer 2**

| | £ |
|---|---|
| Salary | 18,000 |
| Medical Insurance (amount treated as earnings) | 500 |
| | 18,500 |
| Living expenses £2,200 | |
| Restricted to: | |
| 10% x £18,500 | 1,850 |
| Total employment income | **£20,350** |

Accommodation is job related so the restriction in s.315 applies.