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Tax deductions in relation to home office expenses

Flexible work arrangements have become increasingly popular as the needs of employers and employees change. There is also financial pressure on employers to reduce overhead costs, such as office space. This is especially relevant right now since many employees are required to work from home in order to reduce the spread of Covid-19, and many employers have chosen to not return to their offices, as advised by the Government, wherever possible. This has created an opportunity for many employees who did not previously claim home office expenses as tax deductions, to do so in the 2021 tax year (1 March 2020 – 28 February 2021), in particular (and possibly going forward) if working arrangements move away from offices and more towards remote working.

The South African Revenue Service (SARS) allows certain taxpayers to deduct their home office expenses from their taxable income, provided that the requirements of the Income Tax Act No. 58 of 1962 (the Act) are met. Interpretation Note 28, Issue 2 (as issued by SARS on 15 March 2011) provides additional guidance on the deductibility of Home Office Expenses. The general rule is that the deductibility of expenses relating to a home office is determined with reference to section 11, paragraphs (a), (d) and (e), read together with sections 23(b) and 23(m). This means that for a home office expense to be deductible the requirements of sections 11, 23(b) ***and*** 23(m) must ***all*** be met.

The below addresses the position of both a self-employed individual or independent contractor, and a person in employment (an employee) earning remuneration.

Sole proprietors and independent contractors

Individuals who are not in employment and who do not receive remuneration may claim pro-rata home office expenses if the home office space is:

- specifically equipped for the purposes of trade; and
- regularly and exclusively used for trade purposes.

Employees

There are two scenarios to consider as relates to employees.

Employees who do not earn mainly commission income

If an employee does not earn mainly (more than 50%) commission income or variable payments, he/she may potentially still be able to claim home office expenses as a deduction against taxable income. These employees must also be able to show that they have worked from their home office for more than 50% of the tax year. They may deduct the pro-rata costs related to rent, interest on a mortgage bond, repairs to the premises, rates and taxes, cleaning, and all other expenses in connection with the dwelling. They may also claim wear and tear as stipulated in Section 11(e) on computer hardware and software, office furniture and office equipment (where owned by the employee and not the employer, for obvious reasons).

Commission earners

Employees earning more than 50% of their total remuneration from commission or some other variable payments, based on work or performance, whose employment duties are mainly (more than 50%) performed from the home office, would be allowed to claim the same expenses as employees who do not earn mainly commission. However, in addition, they may claim other commission-related business expenses, such as telephone, data costs, stationery and repairs to the printer.

Calculation of the home office expense deduction

The qualifying home office expenses are tallied for the tax period impacted. The home office claim is calculated as a percentage of the square metres of the home office over the total square metres of the entire dwelling. It is important to note that some costs are not subject to the pro-rata formula e.g. wear and tear on office equipment (the calculation for wear and tear is specifically stipulated in Section 11(e) of the Act).

Claiming home office expenses on the annual income tax return (form ITR12)

The calculated home expense deduction should be included under the “Deductions” section on the ITR12 form. It is important for the taxpayer to retain supporting documents that may be required by SARS for a period of five (5) years in order to validate the deduction claimed. Given the expected increase in home office claims for the 2021 tax year, it is likely that SARS will require the uploading of supporting documents for all such claims and may seek to audit the expenses claimed in many cases.

Reimbursement of office equipment purchased for the home office

Where an employee purchases a home office asset and the asset remains the asset of the employee, the reimbursement of this cost by the employer is a taxable benefit and will be subject to employees’ tax withholding. However, where an employee purchases a home office asset for exclusive use for work purposes (e.g. an office chair) and is reimbursed by the employer (where the asset remains the property of the employer but is used by the employee), this will not be considered a taxable benefit.

Capital gains tax implications

When a taxpayer disposes of an asset such a house or property, a capital gains tax event arises. Where a residence is partly used for business purposes (such as a home study), the primary residence exclusion must be reduced by taking into account the period of business use as well as the size of the area used for business purposes. This should be taken into consideration when claiming this deduction, as it may create a higher capital gain in the employee’s hands later on sale of the property.

Attached is Annexure B to Interpretation Note 28, which is an effective guide to make decisions regarding qualifying expenses.

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