What is the trading allowance?

The trading allowance is an allowance of up to £1,000 per tax year which can be used against your trading, casual or other miscellaneous income to exempt it from income tax. It is available from the 2017/18 tax year onwards. It is not an automatic allowance like the personal allowance and so may need to be specifically claimed in some circumstances.

Who can use it?

If you are an individual, who is not trading as part of a partnership, you can use the trading allowance if you have trading, casual or other miscellaneous income. Trading income is income from self-employment, this can be from buying and selling goods or from services, for example gardening, delivery or taxi driving. Casual income includes things like hiring out equipment and also includes income from the ‘sharing economy’ such as car sharing. If you are trading through a limited company then you can’t use the trading allowance.

Wherever trading income is mentioned elsewhere in this factsheet it is assumed to include casual or miscellaneous income too.
How do I get the trading allowance if my total trading income (before deducting any expenses) is more than £1,000?

This is when your total trading income is more than £1,000 and you can claim the trading allowance to reduce this income by £1,000 instead of claiming any business expenses. For example, if you run a dog-walking business and you make £1,400 during the tax year and have expenses of £150 then you can claim the trading allowance of £1,000 instead of your business expenses of £150 (you cannot claim both!) and your taxable income will only be £400 instead of £1,250.

As your income is above the trading allowance you must register with HMRC and complete a Self Assessment tax return. You can claim the trading allowance when you complete your tax return on page 1, box 10.1 on the self-employment (short) pages (SA103S) of the tax return by completing box 10.1 to show the amount you are claiming.

If you have more than one trade or source of casual income, then you can decide how to allocate the trading allowance between the different income streams. However, it is not always beneficial to get the trading allowance, and below we explain other factors you should consider before deciding to claim it.

What records should I keep if I am using the trading allowance?

You should still keep records of your trading income and expenses so you can work out whether or not you are entitled to use the trading allowance, and if so, whether you want to do so. There is guidance on record keeping on the LITRG website:

www.litrg.org.uk/tax-guides/self-employment/business-records
Why might I not want to claim the trading allowance?

On the face of it, it sounds like there should be no reason not to use the trading allowance; however, it may not be beneficial for you to do so in certain circumstances. These include:

- You have business expenses greater than £1,000. In this case you will have less taxable profit if you deduct your expenses from your trading income rather than the trading allowance and therefore will pay less tax!

- You have made a trading loss. If your expenses are greater than your income, it will be beneficial to complete a Self Assessment tax return and make a claim for the losses rather than use the trading allowance. We explain about losses on our LITRG website: [www.litr.org.uk/tax-guides/self-employment/working-out-profits-losses-and-capital-allowance/what-if-i-make-loss](http://www.litr.org.uk/tax-guides/self-employment/working-out-profits-losses-and-capital-allowance/what-if-i-make-loss)

- You have more than one trading business and/or type of casual income. In this case you need to ensure that your total expenses are less than £1,000 otherwise you could end up paying more tax, see the example below.

Example

For example, Jay is self-employed as a graphic designer and has sales of £25,000 and expenses of £1,500 for the 2020/21 tax year, making a profit of £23,500. She also makes gift cards and has sales of £900 and associated business costs of £800. Jay does not realise that the trading allowance must be applied to all her self-employed activities and makes a claim for the trading allowance, assuming it will just go against her card-making business only. However, this is not the case and by claiming the allowance she will only get a deduction for £1,000 rather than her actual expenses of £2,300. Therefore, unless she amends her tax return she will miss out on tax relief on £1,300 of business expenses (£1,500 + £800 = £2,300 less £1,000 allowance = £1,300). Assuming Jay is a basic rate taxpayer this error could cost her extra tax of £260 as well as extra Class 4 National Insurance contributions.

Don’t forget Class 2 National Insurance!

Some self-employed people earn profits less than the **Small Profits Threshold**, which is £6,475 for the 2020/21 tax year (£6,365 for the 2019/20 tax year), and so do not have to pay flat-rate Class 2 National Insurance contributions (NIC). However, some self-employed taxpayers choose to pay Class 2 NIC to build up their entitlement to certain state benefits such as the state pension and maternity allowance. There is more information on what benefits Class 2 NIC counts towards on our website: [www.litr.org.uk/tax-guides/tax-basics/what-national-insurance#toc-what-benefits-do-my-contributions-pay-for](http://www.litr.org.uk/tax-guides/tax-basics/what-national-insurance#toc-what-benefits-do-my-contributions-pay-for).

If you decide to pay Class 2 NIC then you will need to register your self-employment and complete a Self Assessment tax return even if your trading income is less than £1,000. You will then need to claim the appropriate amount of trading allowance on your tax return in box 10.1 of the self-employment (short) pages (SA103S).
How does the trading allowance work with tax credits and universal credit?

If you claim tax credits, the income used to calculate your tax credits should be after taking account of any deduction for the trading allowance; this is because the information about your income which you provide to HMRC for your tax credits claim will generally be the same as the information you use when completing your Self Assessment tax return. If you do not need to register your trading income with HMRC because it is under £1,000 then you will not need to let the HMRC tax credits team know about it either.

Universal credit (UC) works differently, and you cannot deduct the trading allowance when providing your income to the Department for Work & Pensions (DWP). The income used when calculating your UC will be higher than the income used when calculating your tax as the trading allowance is ignored when calculating your UC claim.

So Sarah has income from hairdressing of £3,000 and expenses of £425, making an accounting profit of £2,575. For income tax purposes she will be entitled to the trading allowance and so her taxable income is £2,000 (£3,000 - £1,000). If she claims tax credits she should report income of £2,000; however if Sarah was receiving UC then she would have to report income received less expenses paid out in her monthly assessment period. The trading allowance would be completely disregarded in calculating her UC award and would make no difference to the figures she needs to report for UC purposes.

What happens if I have a student loan?

If you have a student loan and also have income covered by the trading allowance, this income is not included when working out whether you have earned above the loan repayment threshold or when calculating the amount of any loan repayments. In other words, the calculation of your loan repayments follows the tax treatment of your trading and casual income. So if you have a Plan 2 loan and employment income of £27,000 and casual income of £750 which is fully relieved by the trading allowance, only £27,000 (and not £27,750) will be used when calculating your student loan repayments above the repayment threshold.

Where can I get more information?

See our trading allowance webpage on the LITRG website: www.litrg.org.uk/tax-guides/self-employment/what-trading-allowance


Claiming Tax-free childcare?

If you want to claim tax-free childcare you still need to register your self-employment and complete a tax return even if your trading income is less than £1,000; see the LITRG website: www.litrg.org.uk/tax-guides/help-towards-costs-childcare/Tax-free-childcare