

Unlocking the Home-Office Deduction

Business owners, **especially individuals who are self-employed**, may use one of two methods of deducting home-office expenses. A lesser-known "simplified" method can provide a flat-dollar write-off without the usual recordkeeping hassles. As a business owner, you may be able to have a larger deduction if you use the traditional "regular" method.

- **Who may deduct home-office expenses** – those of you who only use a portion of your home regularly and exclusively as your principal place of business or a place to meet or deal with customers, clients, or patients in the normal course of business.
- In addition, you may deduct expenses for a **business storage area or a separate structure** (e.g., a detached garage or barn) used only for business purposes.
- To claim a deduction, you may use the regular method or the recently-approved simplified method.
Regular method -- You must compute the business use of the home by separating the expenses of operating the home between personal and business use. Ask your tax preparer for further explanation of direct business expenses which are fully deductible and indirect total expenses.
Simplified method -- This method reduces the paperwork and recordkeeping burden for small businesses. It has a prescribed rate of \$5 a square foot for business use of the home up to 300 square feet, for a maximum annual deduction of \$1,500. Choosing this option requires taxpayers to complete a short worksheet in the tax instructions and enter the result on the tax return. There is a special calculation for daycare providers.
- Regardless of the method used to compute the deduction, **business expenses in excess of gross income aren't deductible.**
- **Deductible expenses for business use of a home include the business portion of:**
 - Real estate taxes
 - Mortgage interest
 - Rent
 - Casualty losses
 - Utilities
 - Insurance
 - Depreciation
 - Maintenance
 - Repairs

In general, expenses for the parts of the home not used for business can't be deducted.

- You also may take a **deduction for business storage purposes** when the dwelling unit is the sole fixed location of the business or is used regularly for providing daycare services. Note: Exclusive use isn't required in these instances.
- Even though the IRS is reminding taxpayers about the simplified option, **you may do better by deducting actual expenses.**
For example, suppose the 200-square-foot room you use for a home office represents 10 percent of the home's total 2,000 square feet. Now say that you have direct expenses of \$2,000 and \$10,000 in indirect expenses (not counting mortgage interest and property taxes, which are generally deductible anyway). Using the regular method, your deduction of \$3,000 ($\$2,000 + 10$ percent of $\$10,000$) is two times the maximum deduction allowed with the simplified method!

Ask your tax preparer to assist you in choosing the best calculation method for your home-office deductions.