



## UNLOCKING the Missed Deductions of a Home Office

Small-business owners should not miss the benefit of a home office deduction out of fear of a tax audit. Going to an office is no longer a requirement of conducting business in the age of the internet, cell phones, Skype and GoTo meetings. This means an increasing number of small-business owners are working from home, and eligible to claim a home office deduction. When properly implemented, this deduction can make a significant difference in your tax liability.

### WHAT CONSTITUTES A HOME OFFICE?

In order to claim a deduction for a home office the IRS requires that a designated space be used exclusively and regularly for business. Exclusively used for business means it cannot ever be used for personal reasons during the tax year, this includes any type of storage for personal items. Although the office is to be used only for business, the tax code does not mandate that it be a separate room, it can be part of a room - walls are not a requirement. The office must also be used on a regular basis for business.

### HOW TO DEDUCT EXPENSES FOR THE HOME OFFICE

There are two different methods you can use to claim a home office deduction, the actual expense method and the simplified method.

#### ACTUAL EXPENSE METHOD

The actual expense method allows you to deduct all direct expenses and a portion of any indirect expenses. Direct expenses are any expenses incurred specifically for the home office, such as painting the office or putting in new

carpet. Indirect expenses include any expenses incurred for the home such as mortgage interest, property taxes and utilities. To claim these indirect expenses you need to determine the portion of the expenses that relate to the home office. This can be calculated by dividing the square footage of the office by the square footage of the house. You can also claim depreciation or a rent deduction for the part of the home used for business purposes. On the downside, when you sell the home any depreciation taken needs be recaptured. This can be an unpleasant surprise come tax time. When using the actual expense method, detailed records and supporting documentation must be kept for all expenses.

#### SIMPLIFIED METHOD

If you prefer not to maintain records of these expenses, you can still take a home office deduction using the simplified method. The simplified method is calculated by simply multiplying the square footage of the office by \$5 per square foot (up to 300 sq. ft.). The advantage to this method is the IRS does not require you to keep any records that are required by the actual expense method. The main drawback of the simplified method, is that you will not be able to deduct your actual expenses if they exceed the allowance of the simplified method.

The best solution is to keep track of all of your expenses and then determine at the end of the year which method will provide the greater deduction.

#### MILEAGE

Regular commuting to and from work is not a deductible expense, however travel between your primary office located in your home to your second office is classified as business miles that are deductible. This does not mean that you can set up a "home office" to deduct your regular commuting miles. It means that if your home office is where you conduct the majority of your business, you can deduct any mileage to a secondary location. Setting up a home office can potentially create several thousands of dollars in deductible mileage each year.

#### TAKE AWAY

Even the smallest home office can unlock significant deductions if the expenses are properly accounted for using either the actual or simplified method. It is very important that the space be used exclusively for business use.

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