



Overview

You might be able to claim a significant tax deduction for the business use of your space. If you're working from the comfort of your own home, whether that's a cozy apartment, a sprawling house, or even a unique living space like a boat, you might be able to save on taxes.

What does it take to qualify? Whether you're storing inventory or using a part of your home as an office, there are specific criteria to meet. Daycare providers, you're in for some special rules tailored just for you.

Once you qualify, you're ready to calculate your deductions. There are two ways to do this: the detailed route of itemizing actual expenses or opting for the simplified method, which will save you time and paperwork.

This brief on [IRS Publication 587, Business Use of Your Home](#), speeds up securing your home office deduction. Pub 587 is 34 pages long. This is compressed so refer to the official publication when making decisions for the most up-to-date policies and procedures.

What you'll learn...

- Qualifying for a Deduction
- Figuring the Deduction
- Recordkeeping

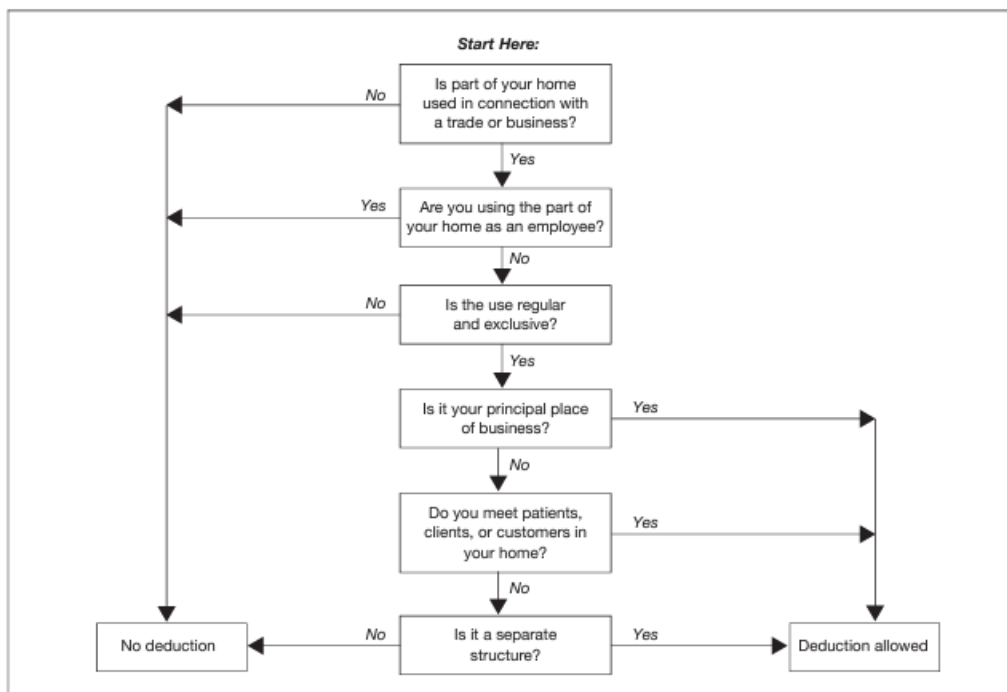
Qualifying for a Deduction

To claim deductions for the business use of your home, you must meet specific criteria. Normally, common home expenses like mortgage interest, real estate taxes, and utilities aren't deductible as business expenses. But, if part of your home is used exclusively and regularly for business purposes, you may be eligible for deductions. This includes using your home as your principal place of business, meeting clients or customers, using a separate structure on your property, or using your home for storage related to your business.

To qualify for home office deductions, the space must be used:

- Exclusively and regularly as your main place of business
- Exclusively and regularly for meeting clients or customers in your trade or business
- For a separate, unattached structure in connection with your business
- Regularly for storage of inventory or product samples
- For rental purposes (see Pub. 527)
- As a daycare facility

Figure A. **Can You Deduct Business Use of the Home Expenses?** Do not use this chart if you use your home for the storage of inventory or product samples, or to operate a daycare facility. See *Exceptions to Exclusive Use*, earlier, and *Daycare Facility*, later.



Exclusive Use Test

To qualify for the home office deduction under the exclusive use test, a specific area of your home must be used only for your trade or business. This area could be a room or another defined space, and it doesn't require a permanent partition to qualify. However, if the space is used for both business and personal activities, it does not meet the exclusive use criterion.

For example, if you are an attorney using your home den to write legal briefs, but your family also uses it for recreation, you cannot claim a deduction for its business use.



Exceptions to the Exclusive Use Test

You can claim home office expenses without meeting the exclusive use test if you use part of your home to **store inventory or product samples** for your business. To qualify, you must:

- Operate a wholesale or retail business,
- Store inventory or product samples at home for business use,
- Have your home as the sole fixed location of your business,
- Use the storage space regularly,
- Utilize a separately identifiable area suitable for storage.

For instance, if you sell mechanic's tools and use half of your basement for storage while occasionally using it for personal purposes, you can still deduct expenses for this space.

If you use part of your home as a **daycare facility**, the exclusive use requirement does not apply.

Outside of these two exceptions, any part of your home used for business must pass the exclusive use test to qualify for deductions.

Regular Use Test

To meet the regular use test, you need to use a designated area of your home for business activities on a consistent basis. Using the space occasionally is not enough. When determining if your usage qualifies as regular, you should assess all relevant facts and circumstances. Regular use is key to establishing that part of your home is genuinely dedicated to your business activities.

Trade or Business Use Test

To pass the trade-or-business-use test, you must use a portion of your home specifically for your trade or business activities. Simply engaging in profit-seeking activities does not qualify unless they are part of an established trade or business.

For example, if you use a part of your home to read financial periodicals and engage in investment-related activities for personal investment purposes, and not as a professional broker or dealer, these activities do not qualify as a trade or business. Therefore, you cannot claim a home office deduction. This test emphasizes the need for the space to be used in connection with a genuine business operation.



Principal Place of Business Test

If you operate a trade or business from multiple locations, including your home, your home may qualify as your principal place of business under certain conditions. To determine if your home office meets this criterion, you should evaluate two key factors:

- **Relative Importance:** Consider the importance of the activities performed at your home compared to other locations where you conduct business.
- **Time Spent:** Assess how much time you spend working from each business location.

Your home office will qualify as your principal place of business if:

- You use it exclusively and regularly for the administrative or management tasks of your business.
- There is no other fixed location where you conduct substantial administrative or management activities for your business.

A Home Office for More Than One Trade or Business

Your home office can serve as the principal place of business for more than one distinct trade or business. However, it's important to evaluate each business activity separately to determine if the office qualifies as the principal place of business for each.

To qualify for deductions for multiple businesses, it must be used exclusively and regularly for the following purposes:

- As the principal place of business for one or more of your trades or businesses.
- As a location to meet or deal with patients, clients, or customers in the normal course of your business activities.
- If the office is a separate structure on your property, it must be used in connection with your trades or businesses.

Home Office Expenses for Meeting Patients, Clients, or Customers

If your home serves as a place where you meet with patients, clients, or customers as part of your business operations, you may be eligible to deduct expenses for the part of your home used for these meetings. This is possible even if you conduct business activities at another location. To qualify for such deductions, you must meet both of the following criteria:

- **Physical Meetings:** You must physically meet with patients, clients, or customers in your home.
- **Substantial and Integral Use:** The use of your home for these meetings must be substantial and integral to the operation of your business.

This requirement is typically met by professionals like doctors, dentists, attorneys, etc., who maintain offices in their homes specifically for these purposes. However, merely using your home for occasional meetings or telephone calls does not qualify for home office deductions. Importantly, the area used for meetings does not need to be your principal place of business, but it must be used exclusively and regularly for business meetings.



Figuring the Deduction

There are two ways for figuring your home office deduction: the simplified method and using actual expenses. You can choose which one to use each year meeting applicable requirements.

Using the Actual Expense Method to Calculate Deductions

If the simplified method is not suitable or available for your situation, calculate your deduction using actual expenses.

- Determine the percentage of your home used for business purposes.
- Calculate the actual expenses associated with that portion, such as utilities, rent, insurance, and depreciation.
- Applying any limitations on the deduction amount.

Part-Year Use: You can only deduct expenses for the part of the year your home was used for business. For example, if you start using your home for business on July 1, only calculate your expenses from July to the end of the year for your deduction.

Calculating Deductions for Actual Expenses

When using actual expenses, you must allocate the costs between personal and business use.

Type of Expense: Is it a direct expense (solely for the business part of your home), an indirect expense (for keeping up and running your entire home), or unrelated to the business use of your home.

Business Use Percentage: The percentage of your home used for business is used to calculate indirect expenses you can allocate towards your home office deduction.

Table 1. Types of Expenses

Expense	Description	Deductibility
Direct	Expenses only for the business part of your home. Examples: Painting or repairs only in the area used for business.	Deductible in full.* Exception: May be only partially deductible in a daycare facility. See Daycare Facility , later.
Indirect	Expenses for keeping up and running your entire home. Examples: Insurance, utilities, and general repairs.	Deductible based on the percentage of your home used for business.*
Unrelated	Expenses only for the parts of your home not used for business. Examples: Lawn care or painting a room not used for business.	Not deductible.

*Subject to the deduction limit, discussed later.



Calculating Business Percentage of Home Use

To accurately claim home office deductions, it's essential to determine the business percentage of your home. This percentage is based on the proportion of your home that is used for business activities and is crucial for calculating the deductible portion of home operating expenses.

Methods for Determining Business Percentage

Use any reasonable method to determine the business percentage. Here are two common approaches:

Area: Calculate the area ($l \times w$) of the space then divide it by the total area of your home. For example, a home office is 100 square feet ($10' \times 10'$) and your total home area is 1000 square feet, your business percentage is 10%.

Room: If the rooms in your home are approximately the same size, divide the number of rooms used for business by the total number of rooms. For example, you use one room as an office and your home has ten rooms, your business percentage is 10%.

Understanding the Limitations

It's important to understand how gross income from your business affects the deductible amount of your home office expenses.

Full Deduction Eligibility: If the gross income from your home-based business equals or exceeds your total business expenses (which include depreciation), you can deduct all your business expenses related to the use of your home.

Deduction Limitations: However, if your business's gross income is less than your total business expenses, the amount you can deduct for certain home-related expenses may be limited.

First, take the gross income from the business use of your home...

Then subtract the business portion of expenses that you would be allowed to deduct regardless of business use:

- Mortgage interest
- Real estate taxes
- Casualty losses related to a federally declared disaster (if you itemize deductions on Schedule A (Form 1040), or net qualified disaster losses if you claim the standard deduction).

Next, subtract other business expenses that are directly related to your business but not to the use of the home itself:

- Business phone expenses
- Office supplies
- Depreciation on business equipment

After subtracting these amounts, the remaining limit is what you can claim for otherwise nondeductible home expenses such as utilities, insurance, and home depreciation. Depreciation of the home is calculated last.



Using the Simplified Method to Calculate Deductions

The simplified method offers an easier way to calculate your home office deductions without needing to track and allocate actual expenses. You calculate your deduction by applying a set rate of \$5 per square foot to the area of your home that's used for business. The maximum area you can use for this calculation is capped at 300 square feet. This straightforward approach minimizes the complexity involved in documenting and substantiating your home office expenses.

Implications of Choosing the Simplified Method

When you opt for the simplified method to calculate your home office deductions, it streamlines the process but comes with specific limitations:

- **Exclusion of Actual Expenses and Depreciation:** Choosing the simplified method means you cannot deduct actual expenses related to the business use of your home, such as utilities, repairs, or depreciation. The depreciation deduction for the portion of the home used for business is considered zero for the year.
- **Non-Business-Related Expenses:** Mortgage interest, real estate taxes, and casualty losses should be treated as personal expenses under the simplified method. If you rent part of your home, these expenses must still be allocated between the rental and personal use, which includes the business use calculated using the simplified method.
- **No Deduction or Carryover of Disallowed Actual Expenses:** If you previously used actual expenses for your home office deduction and some of that deduction was disallowed, you cannot deduct the carried-over amount in the year you choose the simplified method. Instead, this disallowed amount must be carried forward to future years when you might switch back to using actual expenses for your deduction.

Switching back to actual expenses in subsequent years requires using the appropriate depreciation tables for Modified Accelerated Cost Recovery System (MACRS) to calculate depreciation. This approach to home office deductions simplifies the process for some but may lead to different financial outcomes depending on your specific expenses and business use of the home.



Recordkeeping

When it comes to deducting expenses, maintaining thorough and organized records is crucial. You are not required to follow a specific recordkeeping method, but your records must be detailed enough to verify your deductions.

- **Proof of Expenses:** Preserve all canceled checks, receipts, bills, and other documents that verify the expenses you're claiming.
- **Usage Details:** Your records should clearly indicate the portion of your home used for business purposes.
- **Nature of Use:** Document that you use this part of your home exclusively and regularly for business, either as your main place of business or as a place where you meet clients or customers in the normal course of your business. Remember to note any exceptions to the exclusive use requirement as discussed previously.
- **Depreciation and Other Expenses:** Keep detailed records of depreciation claimed and all other expenses related to the business use of your home.

Keep records for as long as they are needed for tax purposes, generally the later of:

- **3 years** after the date you filed your return or the return's due date.
- **2 years** after the date you paid the tax.

Depreciation of you home:

- **Depreciable Basis** needs records showing the purchase price, the cost of any improvements, dates of purchase, and how you acquired your home. These records are essential for calculating depreciation.
- **Forms and Worksheets to** retain are Forms 8829 or the Worksheet To Figure the Deduction for Business Use of Your Home, which can serve as records of your depreciation calculations.

For more detailed guidelines on recordkeeping practices, refer to IRS Publication 583, "Starting a Business and Keeping Records." By keeping accurate and comprehensive records, you can ensure that you are prepared to substantiate your home office deductions in the event of an IRS inquiry or audit.