

CORNERSTONE FINANCIAL SOLUTIONS

Individual/Corporate Taxes – Small Business Accounting – Financial Planning



HOME OFFICES & TAXES



A popular late night television program presents the "Top Ten List". Here are ten tax rules that you should be aware of before you start your own home office.

1. **Under new management.** You may qualify for the deduction if you use space in your home exclusively and regularly for administrative or management activities of your trade or business, and you have no other fixed location where you conduct substantial administrative or management activities.
2. **Employees Rule.** The rules for employees are much more stringent, so, as an employee you would only qualify if the space in your home were for the "convenience of your employer". Chances are if your employer provides you space at their offices, the office at home is for your convenience, not theirs and would not be deductible.
3. **Inventory is not exclusive.** Space in your home used to store inventory for your business or job, does not have to be used exclusively for just the inventory. You may still be entitled to the deduction if you use the space to store personal things as well.
4. **Kid Space.** Part of your home that is used as a day care also does not have to be used exclusively for the day care, after hours you may use that space as living quarters as well and still qualify for the deduction. However, any day care space that is not exclusive will be prorated based on hours of use as well as the square footage used.
5. **Direct Expenses in Full.** Expenses for a home office that are 100% related to the business use of a portion of your home are fully deductible. For example the cost of an additional telephone line to your home for a fax would fully deductible.
6. **Indirect Expenses are prorated.** Expenses that benefit the entire home must be prorated for the business portion and the personal portion in the ratio that the business square footage has to the total square footage in the home. For example the cost of insurance would be allocated between the deductible business portion and the non-deductible personal portion.
7. **No Losses.** None of the rules regarding the deduction for a home office will make any difference if your business does not make any money. Home office expenses are only deductible to the extent that you have a profit from the business, you will not be allowed to create or increase a loss from a business with home office expenses.
8. **Depreciation.** If you own your home, you may be able to claim a deduction for depreciation for the portion of your home used for business. Depreciation is an allowance for the wear and tear on the part of your home used for business. Besides allocating the purchase price of your home between the business portion and the personal portion, you will also need to allocate the portion of your purchase price that relates to land your home is on, since land is not depreciable. The annual depreciation rates are fixed by the IRS and basically reflect a process that would deduct the business cost of your home over 39 years.
9. **The tax shelter in a home office.** One of the best tax shelters available is the exclusion of gain that results from the sale of a personal residence. Under rules adopted by the IRS at the end of 2002, having a home office does not minimize the benefit of the gain exclusion. The gain on the entire residence, including the home office, is eligible for the exclusion.
10. **Depreciation ricochet.** Even though the gain on the sale of your home, including the home office, is excludable, any depreciation claimed on the home after May 6, 1997 will still be taxable income in the year of the sale.

If you have any questions on this or any other tax related topic, please feel free to call my office.

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