

HOW TO MAXIMIZE THE TAX BENEFITS OF WORKING FROM HOME

6 CRITICAL
QUESTIONS ASKED
BY EMPLOYEES &
EMPLOYERS



BATTERSHELL & NICHOLS
A PROFESSIONAL SERVICE CORPORATION



CPA

How can you make the most of your home office deductions?

The pandemic forced millions of people to work from home, ushering them into a whole new work environment to which many employees and employers are still discovering and adapting. A vital part of this adaptation involves your taxes.

Whether you are a business owner or an employee, there are tax benefits available to those who are working from home that you do not want to miss.

However, this can be difficult. Tax regulations are **complex** and **changing faster than ever**.

For example, in late 2017, Congress passed the Tax Cuts and Jobs Act, sweeping tax legislation that brought many changes affecting taxpayers for years 2018-2025. This included both the business use of home office deductions and employee reimbursements from employers.

Big changes like this make it hard to feel certain you are taking maximum advantage of available tax provisions.

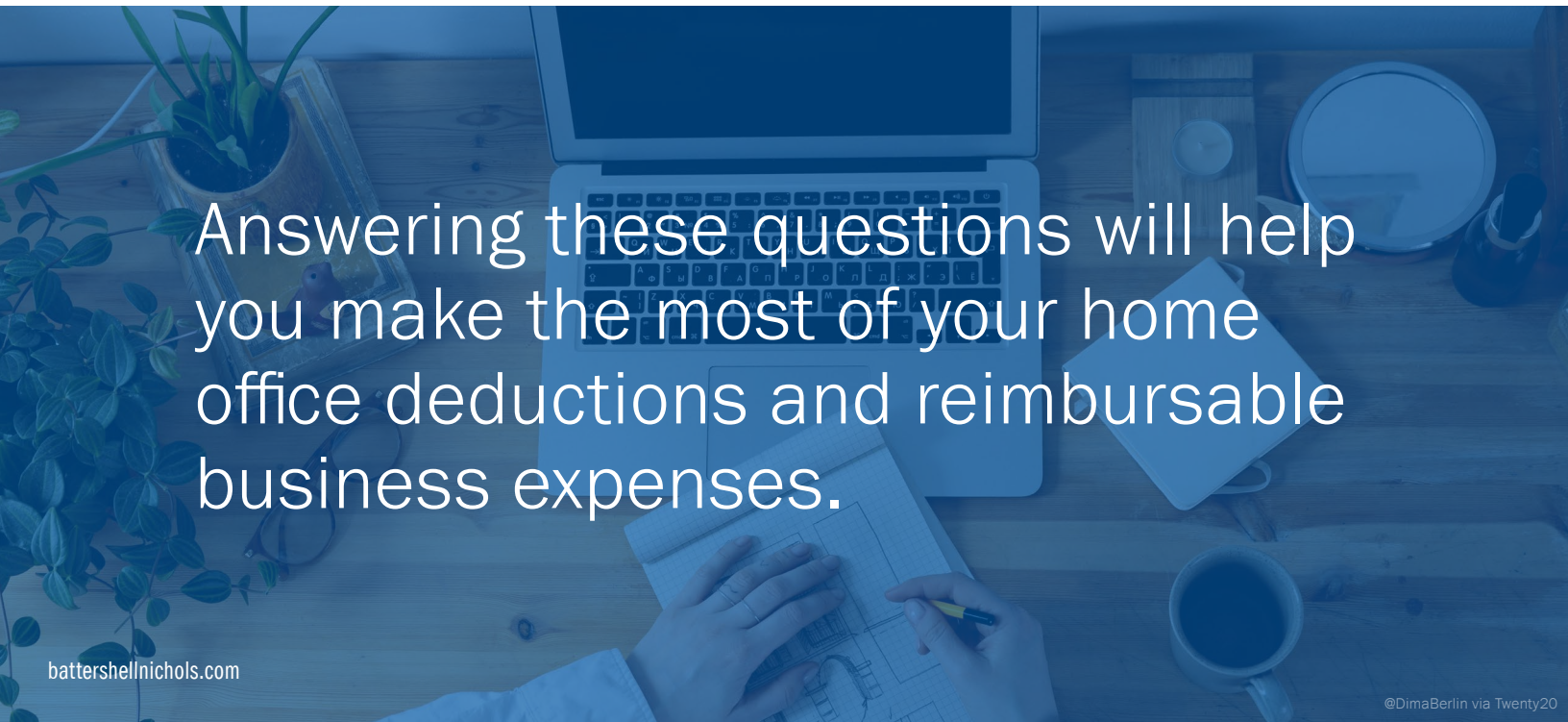
Since 1992, Battershell and Nichols has helped hundreds of clients to navigate complexity and change in order to file their returns with confidence while maximizing tax benefits. We understand the challenges you are facing, and this guide* will help answer your tax questions about working from home.

** The information in this document is subject to revision as rules and regulations change periodically. See our disclosure at the end of this document.*

**There are
six critical
questions
you need to
answer**

1. Does my home office qualify as “business use of home” for tax purposes?
2. If so, what home expenses are tax deductible?
3. How do I calculate my deduction?
4. Where do I take the home office deduction on my tax return?
5. For employees, what expenses are reimbursable by an employer tax-free?
6. Will I be taxed for business expense reimbursements?

Answering these questions will help you make the most of your home office deductions and reimbursable business expenses.



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COVID-19 pandemic was declared a natural disaster.

Unique Tax Benefit Due to COVID-19

The COVID-19 pandemic was declared a natural disaster that allows employers to provide relief payments to employees tax-free under Internal Revenue code section 139. This means these relief payments to employees are not treated as taxable wages, and the employer gets a deduction for the payment. See the “bonus” section near the end of this document to learn more about this little-known provision.

The employer gets a deduction for these payments.

QUESTION ONE

Does my home office qualify for “business use of home” for tax purposes?

QUESTION ONE

DOES MY HOME OFFICE QUALIFY FOR “BUSINESS USE OF HOME” FOR TAX PURPOSES?

There are several qualifications your home office space must meet in order for a sole proprietor or certain owners of partnership interests to qualify for the “business use of home” deduction:

- 1. EXCLUSIVE USE** The home office must be used exclusively in your trade or business; the space may not be used for personal activities. This means if your office doubles as a space for your children to do homework, an area for watching TV, or for a personal side-business, your office would not meet the exclusive use test. There are exceptions to the exclusive use test for daycare businesses.
- 2. REGULAR USE** Your home office must be used frequently for conducting business activities. Occasional use of the office would not be considered regular use.
- 3. BUSINESS USE** Your home office must be used for business purposes and not for personal purposes or another non-business profit-seeking opportunity such as investing. Other duties such as billing, bookkeeping, ordering supplies, and composing reports are all considered business functions.

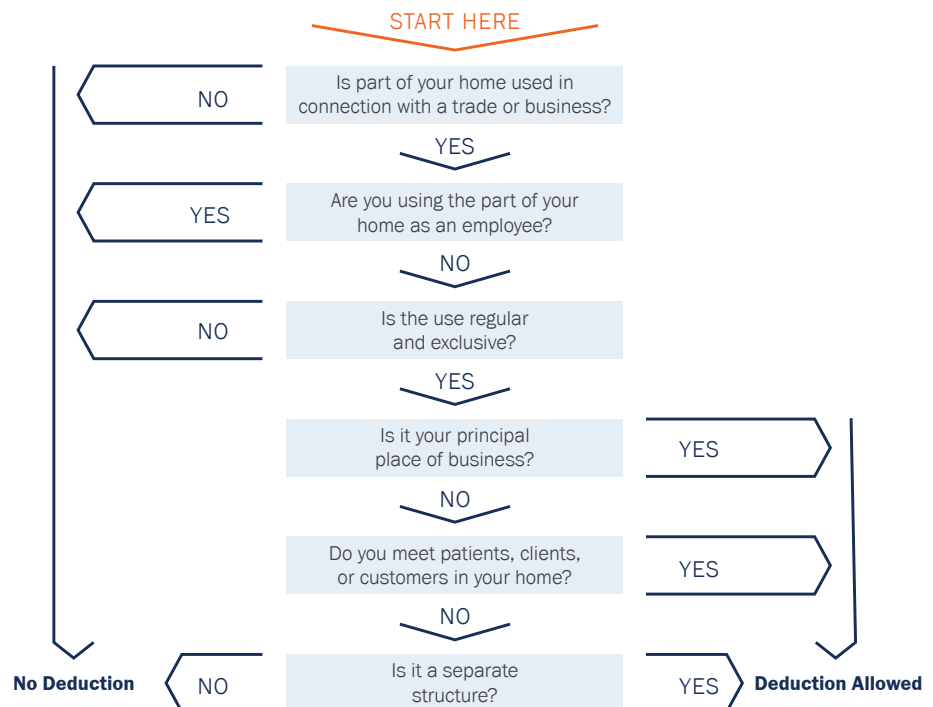
QUESTION ONE

CONTINUED

4. **PRINCIPAL PLACE OF BUSINESS** In order to qualify as a principal place of business, the office must be used exclusively and regularly to perform administrative and management duties. There are several types of activities that, if performed outside of the home office, could disqualify your office under the principal place of business test. This includes:

- Regularly conducting administrative or management meetings at other locations,
- Frequently performing business activities at another fixed location, or
- Having another suitable space to perform administrative activities, but choosing to use your home office instead.

The IRS Publication 587 offers this flowchart to help determine if you qualify for business use of the home:



QUESTION TWO

What home expenses are tax deductible?

QUESTION TWO

WHAT HOME EXPENSES ARE TAX DEDUCTIBLE?

There are three types of expenses, but only the first two are deductible by sole proprietors or certain owners of partnership interests:

- 1. DIRECT EXPENSES** include **costs for the part of your home** that is used exclusively for business. These are fully deductible. This includes painting or repairs for the area of your home used 100% for business.
- 2. INDIRECT EXPENSES** are the **cost of providing for and maintaining the entire home**. Examples include mortgage interest (or rent), real estate taxes, utilities, insurance, casualty losses, and depreciation. Only a certain portion of indirect expenses are included in your calculation, as discussed in the next section.
- 3. UNRELATED EXPENSES** are those related to **parts of your home not used for business** and include repairs and painting outside of your office space and landscaping. These are not deductible and should not be included in the calculation of your home office deduction.

QUESTION THREE

How do I calculate my deduction?

QUESTION THREE

HOW DO I CALCULATE MY DEDUCTION?

There are two approaches to calculating your deduction: the **Actual** and **Simplified** methods.

ACTUAL EXPENSES METHOD

Your deduction will consist of direct and indirect expenses. In order to determine your indirect expenses, **calculate the percentage of your home exclusively used for business (subsequently referred to as office space).**

Do this by dividing the square footage of your office space by the total square footage of your home. This percentage will be applied to your indirect expenses.

- **Example:** If your house is 2,000 square feet and your office space is 200 square feet, the business percentage use of the home would be 10% ($200 / 2,000$).

Depreciation expenses related to your home are more complex. The land is never depreciable, only the allocated cost of the buildings can be depreciated.

To calculate depreciation, you will need to know the following information:

1. The year and month you began using your home office for business purposes.
2. The adjusted basis and fair market value of your home when you started using it for business. The adjusted basis is generally cost plus

QUESTION THREE

CONTINUED

permanent improvements (i.e. electrical or plumbing replacements, new roof, or remodeling), less any casualty losses or depreciation deducted in previous tax years.

Important note: Your home office deduction is limited to the taxable income of your business before the home office deduction. Excess home office deductions can be carried over to future years.

SIMPLIFIED METHOD

The simplified method is **to deduct \$5 per square foot of your office space, limited to 300 square feet, for a maximum home office deduction of \$1,500.**

Note that if you use the simplified method, you cannot take depreciation on your house for that year.

If you calculate your home office deduction using the simplified method one year and the actual expense method the next, you may want to contact our office regarding the depreciation calculation.

QUESTION FOUR

Where do I claim the home office deduction on my tax return?

QUESTION FOUR

WHERE DO I CLAIM THE HOME OFFICE DEDUCTION ON MY TAX RETURN?

If your home office qualifies for the deduction, you will use [Form 8829 “Expenses for Business Use of Your Home”](#) to determine the deduction for the “actual use method”. The deduction calculated on Form 8829 is then reported on [Schedule C “Profit or Loss from Business”](#).

If you use the “simplified method,” the deduction is reported directly on Schedule C. Certain owners of partnerships generally use Schedule E – contact one of our professionals for more information.

QUESTION FIVE

For employees, what expenses are reimbursable by an employer?

QUESTION FIVE

FOR EMPLOYEES, WHAT EXPENSES ARE REIMBURSABLE BY AN EMPLOYER?

Prior to 2018, unreimbursed business expenses were deductible on the 1040 tax return, subject to the 2% adjusted gross income limit. However, when the Tax Cuts and Jobs Act of 2017 was passed, the ability to take miscellaneous itemized deductions for unreimbursed business expenses was suspended.

There are various types of business expenses paid by employees that may be reimbursed by the employer tax-free. The following are common types of reimbursable expenses:

- Travel expenses such as airfare, lodging, and meals
- Dues to professional societies
- Work-related education, conferences, and professional journals
- Equipment and supplies used in performing work for the employer

This is good news for the employee. However, the employer must establish an accountable plan that meets these four IRS requirements:

- 1. BUSINESS PURPOSE** An employee's purchases **must have a direct connection** to performing essential business services for the employer.

QUESTION

FIVE

CONTINUED

- 2. ADEQUATE ACCOUNTING** The employee **must provide a receipt or statement of expense** to their employer within 60 days after the cost was paid or incurred.
- 3. RETURN EXCESS REIMBURSEMENTS** Any reimbursed amount exceeding the actual amount of the business expense is considered an excess reimbursement and **should be returned within a reasonable amount of time.** The IRS defines a reasonable amount of time as within 120 days of when the reimbursement was paid.
- 4. NO REDUCTION IN SALARY** Expense reimbursements should come from the employer's funds and **should not result in a reduction of the employee's salary.**

If the reimbursement plan meets all these requirements, employee reimbursements will generally be non-taxable.

It is important for the employer to have their accountable plan in writing.

SPECIAL RULES FOR CELL PHONES

[IRS Notice 2011-72](#) provides guidance on the tax treatment of cell phones that employers provide their employees for business-use purposes. When an employer provides an employee with a cell phone primarily for non-compensatory business reasons, or reimburses for a reasonable business portion of the employees cell phone costs, these are tax-free benefits.

QUESTION SIX

Will I be taxed for business expense reimbursements?

QUESTION SIX

WILL I BE TAXED FOR BUSINESS EXPENSE REIMBURSEMENTS?

Any valid business expense that is reimbursed under an “accountable plan” will be non-taxable and will not be considered wages to the employee. Expenses that do not meet these requirements are reported as wages on the employee’s Form W-2.

BONUS

A rare tax benefit due
to COVID-19

BONUS

A RARE TAX BENEFIT DUE TO COVID-19

[Internal Revenue Code Section 139 \(Sec. 139\)](#) provides a tax benefit for qualified disaster relief payments. Since the COVID-19 pandemic has been declared a natural disaster, there are expenses incurred by an employee that employers can reimburse “tax free” such as costs to enable the employee to work from home including the cost of a computer, cell phone, printer, supplies, child care or tutoring due to school closures, and more.

While there are no explicit rules to qualify for a disaster relief program, it would be wise for employers to document their intentions to make payments covered by Sec. 139 so that they can inform employees about the parameters of the program in the COVID-19 context. This is a valuable benefit to both employers and employees in this time of great need in our country.

If you would like to discuss this further, please contact our office.

NOW WHAT?

We are to help you!

We are Here for You

We hope this resource sheds light on the tax advantages of the business use of the home deduction and reimbursable employee expenses.

Like all tax laws, things can and do change over time. We keep up to date on the complex and changing tax regulations so you don't have to and we are here to help you.



1. TALK TO OUR TEAM

Get to know us while we make sure we understand your questions and concerns.



2. BE GUIDED THROUGH THE PROCESS

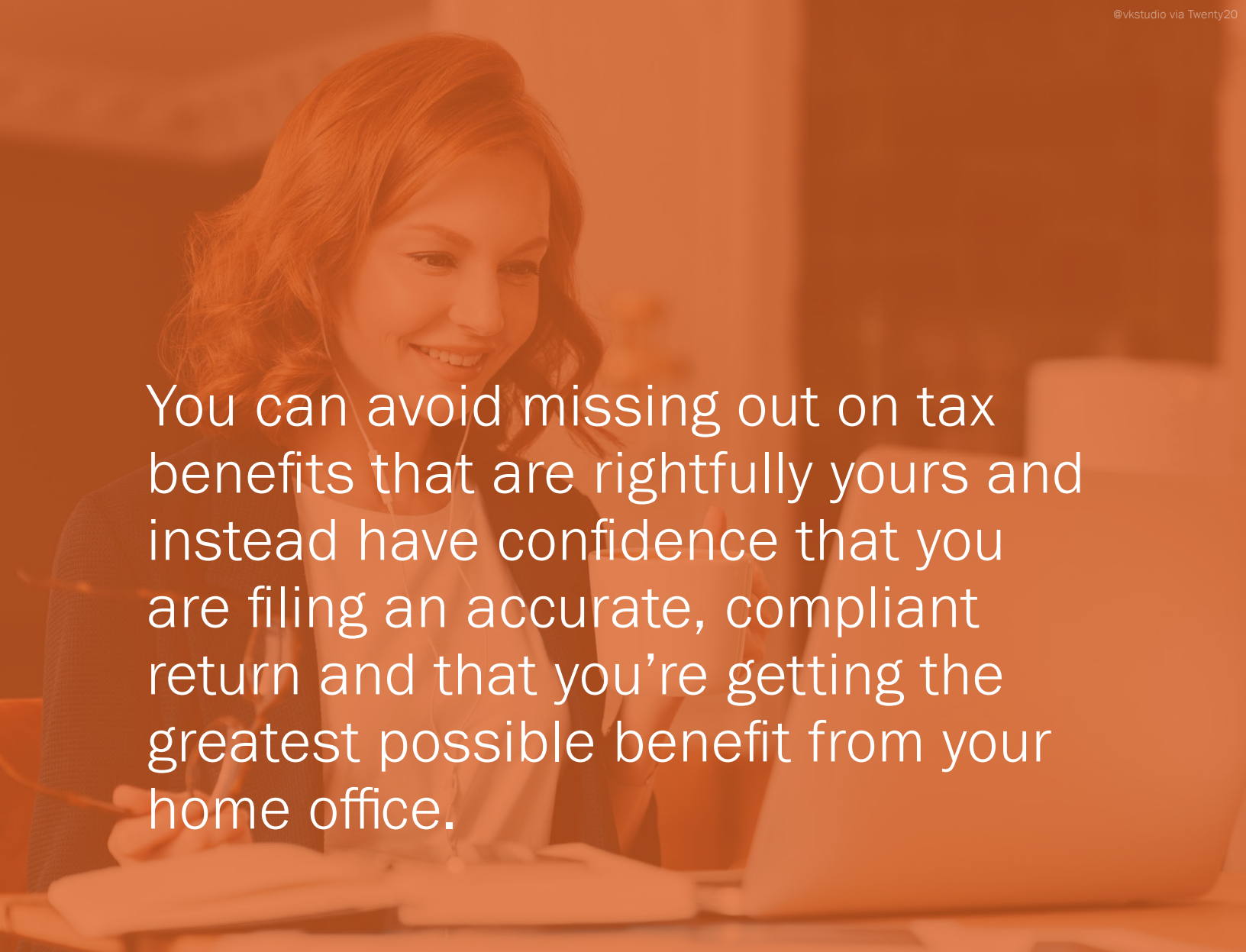
We will make sure you understand the steps needed to minimize your taxes and complete your return.



3. FIND PEACE OF MIND

Know you are maximizing tax benefits while filing an accurate return with a solid plan in place for the future.

This is not just our job. We view it as a calling to help you succeed, and we invest in long-term relationships with our clients. Schedule your free consultation by [emailing us](#) or calling us directly at **253.839.1620**.



You can avoid missing out on tax benefits that are rightfully yours and instead have confidence that you are filing an accurate, compliant return and that you're getting the greatest possible benefit from your home office.

Additional Resources

For the IRS rules and instructions on business use of the home, read [IRS Publication 587](#).

To learn more about accountable plans, see [this article](#) from the Journal of Accountancy.

For IRS rules on deductible business expenses, read [IRS Publication 535](#).

Tax and accounting regulations are complex and changing faster than ever, and the confusion is distracting. At Battershell & Nichols, we come alongside you as a trusted advisor to provide clarity and solutions so you can focus on what matters most.



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