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Business 101 for Translators & Interpreters

Do I Qualify for a Home Office Deduction?

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The home office deduction is a great way to save money on your taxes. On your tax return, you will subtract your deductions from your income, and thereby reduce the amount of income subject to tax.

Both Terri the Translator and Inez the Interpreter qualify for the home office deduction, so let's see what this deduction entails and what the advantages and disadvantages are.

General Concept

By taking the home office deduction, Terri & Inez are able to deduct the expenses related to their offices at home where they conduct their translation and interpreting businesses.

What conditions are necessary for Terri & Inez to qualify? In IRS Publication 587, it says that 3 conditions are necessary to qualify:

1. You must use a room inside your home, or an area within the room, exclusively for business purposes.
2. You must use the room or area regularly for business purposes.
3. The room or area must be your principal place of business.

Terri uses the den next to the kitchen in her house that she owns as her translation office. She uses the entire room:

1. exclusively for business purposes. This means that she uses the room only for the purposes of her translation business. She does not go in there to do her hobbies, use it as a storage area for things not related to translation, nor does she let her children go in there to play;
2. regularly for business purposes. This means that she uses it 5 days a week, 50 weeks out of the year for business; or maybe she uses it 3 times a week for 30 weeks out of the year for business because she has cut back on the hours that she works; and
3. as her principal place of business. This means that it is the main (probably only) translation office that she has.

Inez uses a part of the 2nd bedroom in the apartment that she rents as her interpreting office. Naturally she goes out to the hospital to do medical interpreting, to the court to do judicial interpreting, and to the attorney's office to do legal interpreting. But she uses a desk, phone, computer and bookshelves in a part of the room so she can do administrative or managerial work related to her business such as the billing, phoning clients to look for work, setting up appointments, keeping financial records, keeping an eye on trends in the interpreting business over the internet, etc. Like her colleague Terri, she uses the area exclusively and regularly for her business, and as her principal place of business.

Advantages of Home Office Deduction

The main advantage is that both Terri and Inez can now deduct expenses related to their offices.

Expenses for a home that is owned: a proportional amount of whole-house expenses such as electricity, gas, property tax, cleaning services, repairs (new roof, installation of a new A/C system), home owners insurance, pest control, condominium dues, security system, etc. Other expenses like snow removal or landscaping are not deductible because no clients go to her home to access her office.

Expenses for a home that is rented: Similar to the expenses for a home that is owned, and also a portion of the rent she pays to the landlord becomes deductible.

Naturally, they cannot deduct the entire amounts of those expenses, but they can deduct the expenses proportional for the space of the office. In other words, if the entire home is 1,500 sq.ft, and the office is 120 sq.ft. [$120 \div 1,500 = 8\%$ is attributable to the office], they can deduct 8% of each of those expenses.

They can also deduct 100% of the expenses directly attributable to improvements to the office only. Those kinds of improvements are things like painting the office space, reconfiguring the lighting in the office space, washing the office windows, etc.

One of the other main advantages of taking a home-office deduction for Inez the Interpreter is that now, deducting her mileage or other transportation expenses to various job sites becomes possible. [I'll devote the entire next article to just this topic.]

Disadvantages of Home Office Deduction

Homeowners: One of the deductions required for homeowners is called depreciation. Basically it is a deduction based on the value of your home. While it is advantageous because it provides the homeowner with a valuable deduction each year, it is disadvantageous because when the homeowner sells her home, she must then pay capital gains tax (about 28%) on the total amount of the depreciation deductions throughout the years on her taxes. This deduction probably ends up being a wash: she gets to deduct it each year, but then she has to pay back the benefit when she sells her house. However all of the other deductions she was able to take, like electricity, gas, etc., are finished and there is no disadvantage there. Also, if deducting mileage is important, having a home office is probably a **must**.

Renters: This deduction is not required for renters because they do not own the property and cannot take a depreciation deduction, so there is no such disadvantage for renters. No other disadvantage is evident.

How to Figure out the Size of your Home

In order to take this deduction, you need to know the sq.ft. size of your office (you actually have to get out a tape measure or other measuring device to measure the length and width) and the sq.ft. size of your entire home.

It is best to have a value for the sq. ft. size of your home that has been determined by an arbitrary third party such as the county assessor (found on the county's website or on your property tax bill), the purchase contract of your home, your rental agreement, etc. If the IRS ever sends you a letter asking you to substantiate the sq.ft. size of your home, you can present that kind of third-party documentation that is irrefutable.

How to Calculate the Deduction

You calculate the deduction on IRS Form 8829 that you can find at www.irs.gov You then carry the deduction over to Schedule C which is where you calculate the income and the rest of the deductions for your T&I business.

Summary of What is Necessary to Take the Home Office Deduction

1. You must pay the expenses in order to deduct the expenses. If you split the expenses with someone who is not your spouse such as another co-owner or co-renter, you can deduct only the portion of the expenses you pay for.
2. You must calculate the size of the office, and you must know the size of the entire home.
3. If you own your home, you must know how much you paid for it plus the value of improvements you have made to the home in order to calculate the depreciation deduction. For example, I bought it in 2005 for \$150,000, and I put \$25,000 in improvements into the house (plumbing, roof & A/C, for example). If you make improvements in 2013 such as a new roof or new A/C system for the whole house, be sure to recalculate the value of your home in your 2013 tax return to include these improvements. If the market price of your home is less than what you have invested in it (for example, a similar home in your neighborhood just sold for \$110,000), you must have a good idea of what the market price is because the depreciation deduction is based on the lower of those two values.
4. If you own your home, you must also know how much you paid in mortgage interest and real-estate taxes because you will deduct a portion of them here, and the remainder on Schedule A Itemized Deductions.