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Business Use of Your Home
(Including Use by Day-Care Providers)

For use in preparing

1998 Returns

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Contents

Important Change for 1998

Increase in the section 179 deduction. If you bought certain property to use in your business, you may be able to elect to deduct (rather than depreciate) all or a part of its cost as a section 179 deduction. For 1998, the total you can elect to deduct is increased to $18,500. In 1999 the total will increase to $19,000. For more information on the section 179 deduction, get Publication 946, *How To Depreciate Property.*

Important Change for 1999

Definition of principal place of business. Beginning in ***1999,*** new rules allow your home office to qualify as your principal place of business for deducting expenses for its use if:

1) You use it exclusively and regularly for the administrative or management activities of your trade or business, and
2) You have no other fixed location where you conduct substantial administrative or management activities of your trade or business.

The expanded definition of principal place of business does not take effect until 1999. For more information, see *1999 Rules for Business Use of Your Home* later in this publication. For the current definition, see

Principal Place of Business under *Qualifying for a Deduction.*

Introduction

The purpose of this publication is to provide information on figuring and claiming the deduction for business use of your home. The publication will help you determine all of the following.

- Whether you qualify to deduct expenses for the business use of your home.
- What types of expenses you can deduct.
- How to figure the deduction (including depreciation of your home).
- What records you should keep.
- Where to deduct your expense.

The term ***home*** includes a house, apartment, condominium, mobile home, or boat. It also includes structures on the property, such as an unattached garage, studio, barn, or greenhouse. However, it does not include any part of your property used exclusively as a hotel or inn.

The publication also includes information on all of the following.

- Special rules for day-care providers.
- Selling a home that was used partly for business.
- Deducting expenses for furniture and equipment used in your business.

If you are an employee or file Schedule F (Form 1040), use the worksheet and its instructions, near the end of this publication, to help figure your deduction. If you file Schedule C (Form 1040), you must use Form 8829, *Expenses for Business Use of Your Home.* The *Schedule C Example* shows how to report the deduction.

If you need information on deductions for renting out your property, get Publication 527, *Residential Rental Property.*

The rules in this publication apply to individuals, trusts, estates, partnerships, and S corporations. They do not apply to corporations (other than S corporations). There are no special rules for the business use of a home by a partner or S corporation shareholder.

Useful Items

You may want to see:

Publication

- ☐ **523** Selling Your Home
- ☐ **551** Basis of Assets
- ☐ **583** Starting a Business and Keeping Records
- ☐ **946** How To Depreciate Property

Form (and Instructions)

- ☐ **2106** Employee Business Expenses
- ☐ **2106–EZ** Unreimbursed Employee Business Expenses
- ☐ **4562** Depreciation and Amortization
- ☐ **8829** Expenses for Business Use of Your Home

See *How To Get More Information* near the end of this publication for information about getting these publications and forms.

Help with unresolved tax issues. Most problems can be solved with one contact by calling, writing, or visiting an IRS office. But if you have tried unsuccessfully to resolve a problem with the IRS, you should contact the Taxpayer Advocate's Problem Resolution Program (PRP). Someone at PRP will assign you a personal advocate who is in the best position to try to resolve your problem. The Taxpayer Advocate can also offer you special help if you have a significant hardship as a result of a tax problem.

You should contact the Taxpayer Advocate if:

- You have tried unsuccessfully to resolve your problem with the IRS and have not been contacted by the date promised, or
- You are on your second attempt to resolve a problem.

You may contact a Taxpayer Advocate by calling a new assistance number, 1–877–777–4778. Persons who have access to TTY/TDD equipment can call 1–800–829–4059 and ask for the Taxpayer Advocate. If you prefer, you can write to the Taxpayer Advocate at the office that last contacted you.

While Taxpayer Advocates cannot change the tax law or make a technical tax decision they can clear up problems that resulted from previous contacts and ensure that your case is given a complete and impartial review. Taxpayer Advocates are working to put service first. For more information about PRP, get Publication 1548, *The Problem Resolution Program of the Internal Revenue Service.*

Qualifying for a Deduction

To deduct expenses related to the business use of part of your home, you must meet specific requirements. Even then, your deduction may be limited.

This section describes the tests that you must meet to qualify for the deduction. Use this section, along with *Figure A,* to decide if you can deduct expenses for the business use of your home.

To qualify to claim expenses for the business use of your home, you must meet the following tests.

1) Your use of the business part of your home must be:

   a) Exclusive (however, see *Exceptions to Exclusive Use,* later),

   b) Regular,

c) For your trade or business, AND

2) The business part of your home must be ***one*** of the following:

   a) Your principal place of business,

   b) A place where you meet or deal with patients, clients, or customers in the normal course of your trade or business, or

   c) A separate structure (not attached to your home) you use in connection with your trade or business.

Additional tests for employee use. If you are an employee and you use a part of your home for business, you may qualify for a deduction for its business use. You must meet the tests discussed earlier ***plus:***

1) Your business use must be for the convenience of your employer, and

2) You ***do not*** rent all or part of your home to your employer and use the rented portion to perform services as an employee.

TIP *Whether your home's business use is for your employer's convenience depends on all the facts and circumstances. However, business use is not considered to be for your employer's convenience merely because it is appropriate and helpful.*

Exclusive Use

To qualify under the exclusive use test, you must use a specific area of your home ***only*** for your trade or business. The area used for business can be a room or other separately identifiable space. The space does not need to be marked off by a permanent partition.

You do ***not*** meet the requirements of the exclusive use test if you use the area in question both for business and for personal purposes.

Example. You are an attorney and use a den in your home to write legal briefs and prepare client tax returns. Your family also uses the den for recreation. Since the den is not used exclusively in your profession, you ***cannot*** claim a business deduction for its use.

Exceptions to Exclusive Use

You do not have to meet the exclusive use test if:

1) You use part of your home for the storage of inventory or product samples (discussed next), or

2) You use part of your home as a day-care facility, discussed later under *Day-Care Facility.*

Storage of inventory or product samples. When you use part of your home for the storage of inventory or product samples, the exclusive use test does not apply. However, you must meet all the following five tests.

1) You keep the inventory or product samples for use in your trade or business.

2) Your trade or business is the wholesale or retail selling of products.

3) Your home is the only fixed location of your trade or business.

4) You use the storage space on a regular basis.

5) The space you use is an identifiably separate space suitable for storage.

Example. Your home is the sole fixed location of your business of selling mechanics' tools at retail. You regularly use half of your basement for storage of inventory and product samples. You sometimes use the area for personal purposes. The expenses for the storage space are deductible even though you do not use this part of your basement exclusively for business.

Regular Use

To qualify under the regular use test, you must use a specific area of your home for business on a continuing basis. You do not meet the test if your business use of the area is only occasional or incidental, even if you do not use that area for any other purpose.

Trade or Business Use

To qualify under the trade or business use test, you must use part of your home in connection with a trade or business. If you use your home for a profit-seeking activity that is not a trade or business, you cannot take a deduction for its business use.

Example. You use part of your home exclusively and regularly to read financial periodicals and reports, clip bond coupons, and carry out similar activities related to your own investments. You do not make investments as a broker or dealer. Since your activities are not part of a trade or business, you cannot take a deduction for the business use of your home.

Principal Place of Business

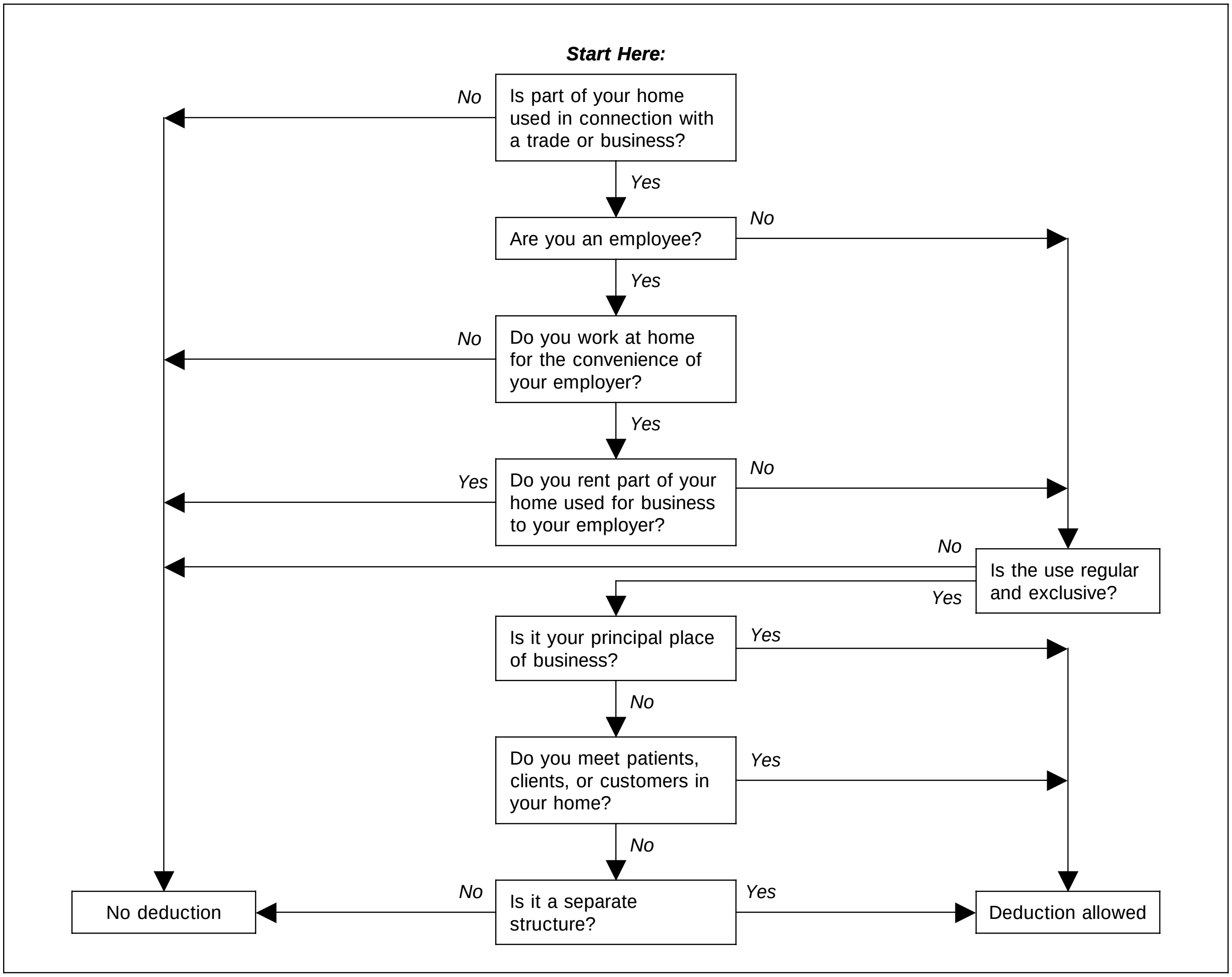
You can have more than one business location, including your home, for a single trade or business. To qualify to deduct the expenses for the business use of your home, your home must be your principal place of business for that trade or business. To determine your principal place of business, you must consider all of the facts and circumstances. If, after considering your business locations, one cannot be identified as your principal place of business, you cannot deduct home office expenses. The following are the two primary factors to consider.

1) The relative importance of the activities performed at each location.

2) The time spent at each location.

Relative importance. To determine whether your home is the principal place of business, consider the relative importance of the activities carried out at each business location. The relative importance of the activities performed at each business location is determined by the basic characteristics of the business.

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 day-care facility. See *Exceptions to Exclusive Use,* earlier, and *Day-Care Facility,* later.

If your business requires that you meet or confer with clients or patients, or that you deliver goods or services to a customer, then:

- The place where you make contact must be given great weight in determining where the most important activities are performed, and
- The performance of necessary or essential activities in your home office (such as planning for services or the delivery of goods, or the accounting or billing for those activities or goods) is ***not*** as important.

Time. If the relative importance of your activities does not clearly establish the principal place of business, such as when you deliver goods or services at both the office in your home and elsewhere, then consider the time you spend at each location. Compare the time you spend on business at your home office with the time you spend at other locations.

Examples of determining the principal place of business. The following examples can help you determine your principal place of business.

Example 1. Jane Williams is a self-employed anesthesiologist. Her only office is a room in her home used regularly and exclusively to do all of the following.

- Contact patients, surgeons, and hospitals by telephone.
- Maintain billing records and patient logs.
- Prepare for treatments and presentations.
- Satisfy continuing medical education requirements.
- Read medical journals and books.

Jane spends approximately 10 to 15 hours a week working in her home office. She spends 30 to 35 hours per week administering anesthesia and postoperative care in three hospitals, none of which provide her with an office.

The essence of Jane's business as an anesthesiologist requires her to treat patients in hospitals. The home office activities, although essential, are less important to Jane's business and take less time than the services she performs in the hospitals. Since her home office is not her principal place of business, she cannot deduct expenses for the business use of her home.

Example 2. Sam Stone is a self-employed plumber. His only office is a room in his home, which he uses regularly and exclusively to phone customers, decide what supplies to order, and review the books of the business. He also employs Helen Green, a full-time unrelated employee, to perform administrative services in his office such as answering the telephone, scheduling his appointments, ordering supplies, and keeping his books.

Sam spends approximately 40 hours a week at his customers' homes and offices, installing and repairing plumbing. He spends approximately 10 hours a week doing work in his home office.

The essence of Sam's trade or business as a plumber requires him to perform services and deliver goods at the homes or offices of his customers. His home office activities, although essential, are less important and take less time than the work he does in the customers' homes and offices. Therefore, his home office is not his principal place of business and he cannot deduct expenses for the business use of the home. The fact that Helen performs administrative activities at his office does not change this result.

Example 3. Joe Smith is a salesperson. His only office is a room in his house used regularly and exclusively to set up appointments, store product samples, and write up orders and other reports for the companies whose products he sells.

Joe's business is selling products to customers at various locations within the metropolitan area where he lives. To make these sales, he regularly visits the customers to explain the available products and to take orders. He makes only a few sales from his home office. He spends an average of 30 hours a week visiting customers and 12 hours a week working at his home office.

The essence of his business as a salesperson requires him to meet with customers primarily at the customer's place of business. The home office activities, although essential, are less important to Joe's business and take less time than the sales activities he performs when visiting customers. Therefore, his home office is not his principal place of business and he cannot deduct expenses for the business use of his home.

Example 4. Fred Jones, a salesperson, performs the same activities in his home office as does Joe Smith in Example 3, except that Fred makes most of his sales to customers by telephone or mail from his home office. He spends an average of 30 hours a week working at his home office and 12 hours a week visiting prospective customers to deliver products and occasionally take orders.

The essence of Fred's business as a salesperson requires him to make telephone or mail contact with customers primarily from his office, which is in his home. Actually visiting customers is less important to his business and takes less time than the sales activities he performs from his home office. Therefore, he can deduct expenses for the business use of his home.

Example 5. Nelson Lewis is employed as a teacher. He is required to teach and meet with students at the school and to grade papers and tests. In addition to a small shared office at the school, he maintains a home office for use in class preparation and for grading papers and tests. He spends about 25 hours per week at the school, and 30 to 35 hours per week at his home office.

The essence of Nelson's work as a teacher requires him to teach and meet with students at the school. Although the class preparation and grading take more time and are essential, they are less important than the activities at the school. He cannot deduct expenses for the business use of his home. Because his home office is not his principal place of business, it is not necessary to determine whether he maintains the office for the convenience of his employer.

More Than One Trade or Business

Whether your home office is the principal place of business must be determined separately for each trade or business activity. One home office may be the principal place of business for more than one activity. However, you will not meet the exclusive use test for any activity unless each activity conducted in that office meets all the tests for the business use of the home deduction.

Example. Tracy White is employed as a teacher. Her principal place of work is the school. She also has a mail order jewelry business. All her work in the jewelry business is done in her home office and the office is used exclusively for the business. If she meets all the other tests, she may deduct expenses for business use of her home for the jewelry business.

If Tracy makes any use of the office for work related to her teaching, she would not meet the exclusive use test for the jewelry business. She may not take any home office deduction for either activity because her job as a teacher does not meet the tests for the deduction.

Place To Meet Patients, Clients, or Customers

If you meet or deal with patients, clients, or customers in your home in the normal course of your business, even though you also carry on business at another location, you can deduct your expenses for the part of your home used exclusively and regularly for business if:

- You physically meet with patients, clients, or customers on your premises, and
- Their use of your home is substantial and integral to the conduct of your business.

Using your home for occasional meetings and telephone calls will not qualify you to deduct expenses for the business use of your home.

Doctors, dentists, attorneys, and other professionals who maintain offices in their homes will generally meet this requirement.

The part of your home you use exclusively and regularly to meet patients, clients, or customers does not have to be your principal place of business.

Example. June Quill, an attorney, works 3 days a week in her city office. She works 2 days a week in her home office used only for business. She regularly meets clients there. Her home office qualifies for a business deduction because she meets clients there in the normal course of her business.

Separate Structure

You can deduct expenses for a separate free-standing structure, such as a studio, garage, or barn, if you use it exclusively and regularly for your business. The structure does not have to be your principal place of business or a place where you meet patients, clients, or customers.

Example. John Berry operates a floral shop in town. He grows the plants for his shop in a greenhouse behind his home. Since he uses the greenhouse exclusively and regularly in his business, he can deduct the expenses for its use, subject to the deduction limit, explained later.

Figuring the Deduction

After you determine that you meet the tests under *Qualifying for a Deduction,* you can begin to figure how much you can deduct. You can deduct certain expenses related to the business use of your home, but your deduction is limited by the following.

- Percentage of your home used for business (business percentage).
- Deduction limit.

This section contains information about the business percentage and deduction limit, and how to adjust your calculations if you use your home for only part of a year.

Business Percentage

To find the business percentage, compare the size of the part of your home that you use for business to your whole house. Use the resulting percentage to figure the business part of the expenses for operating your entire home.

You can use any reasonable method to determine the business percentage. The following are two common methods you can use to figure the percentage.

1) Divide the area (length multiplied by the width) used for business by the total area of your home.
2) Divide the number of rooms used for business by the total number of rooms in your home. You can use this method if the rooms in your home are all about the same size.

Example 1.

- Your office is 240 square feet (12 feet × 20 feet).
- Your home is 1,200 square feet.
- Your office is 20% (240 ÷ 1,200) of the total area of your home.
- Your business percentage is 20%.

Example 2.

- You use one room in your home for business.
- Your home has four rooms, all of about equal size.
- Your office is 25% (1 ÷ 4) of the total area of your home.
- Your business percentage is 25%.

TIP *Use lines 1–7 of Form 8829, or lines 1–3 on the worksheet near the end of this publication, to figure your business percentage.*

Part-Year Use

You cannot deduct expenses for the business use of your home incurred during any part of the year you did not use your home for business purposes. For example, if you begin using part of your home for business on July 1, and you meet all the tests from that date until the end of the year, consider only your expenses for the last half of the year in figuring your allowable deduction.

Deduction Limit

If your gross income from the business use of your home equals or exceeds your total business expenses (including depreciation), you can deduct all your business expenses. If your gross income from that use is less than your total business expenses, your deduction for certain expenses for the business use of your home is limited.

Your deduction of otherwise nondeductible expenses, such as insurance, utilities, and depreciation (with depreciation taken last), allocable to business is limited to your gross income from the business use of your home minus the sum of the following.

1) The business part of expenses you could deduct even if you did not use your home for business (such as mortgage interest, real estate taxes, and casualty and theft losses, which are discussed under *Deducting Expenses,* later).
2) The business expenses that relate to the business activity in the home (for example, salaries or supplies), but not to the use of the home itself.

If you are self-employed, do not include in (2) above your deduction for half of your self-employment tax.

Carryover of unallowed expenses. If your deductions are greater than the current year's limit, you can carry over the excess to your next tax year. They are subject to the gross income limit from the business use of your home for the next tax year. The amount carried over will be allowable only up to your gross income in the next tax year from the business in which the deduction arose, whether or not you live in the home during that year.

Figuring deduction limit and carryover. If you are an employee or file Schedule F, *Profit or Loss From Farming,* use the worksheet near the end of this publication to figure your deduction limit and carryover. If you file Schedule C, figure your deduction limit and carryover on Form 8829.

Example. You meet the requirements for deducting expenses for the business use of your home. You use 20% of your home for this business. In 1998, your gross income, business expenses, and expenses for the business use of your home are deducted in the following order.

Gross income from business	$6,000
Less: Deductible mortgage interest and real estate taxes (20% allowable as business part)	3,000
Balance	$3,000
Less: Business expenses not related to the use of your home (business phone, supplies, and depreciation on office equipment)	2,000
Gross income limit	$1,000
Less: Other expenses allocable to business use of home:	
1) Maintenance, insurance, and utilities (20%)	800
Limit on further deduction	$200
2) Depreciation (20%)	1,600
Depreciation carryover to 1999 (subject to gross income limit in 1999)	$1,400

You can deduct all of the business part of your deductible mortgage interest and real estate taxes ($3,000). You also can deduct all of your business expenses not related to the use of your home ($2,000). Additionally, you can deduct all of the business part of your expenses for maintenance, insurance, and utilities, because the total ($800) is not more than the $1,000 gross income limit. Your deduction for depreciation for the business use of your home is limited to $200 ($1,000 minus $800) for 1998 because of the gross income limit. You can carry over the $1,400 balance and add it to your depreciation for 1999, subject to your 1999 gross income limit.

More than one place of business. If part of the gross income from your trade or business is from the business use of part of your home and part is from a place other than your home, you must determine the part of your gross income from the business use of your home before you figure the deduction limit. In making this determination, consider the time you spend at each location, the business investment in each location, and any other relevant facts and circumstances.

Deducting Expenses

If you qualify to deduct expenses for the business use of your home, you must divide the expenses of operating your home between personal and business use. This section discusses the types of expenses you may have and gives examples and brief explanations of some of the expenses you may be able to deduct.

Types of Expenses

The part of a home operating expense that you can use to figure your deduction depends on:

- Whether the expense is direct, indirect, or unrelated, and
- The percentage of your home that is used for business.

The table below describes the types of expenses you may have and the extent to which they are deductible.

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

*Subject to the deduction limit.

TIP *Form 8829 and the deduction worksheet (both illustrated near the end of this publication) have separate columns for direct and indirect expenses.*

Expenses related to tax-exempt income. Generally, you cannot deduct expenses that are related to tax-exempt allowances. However, if you receive a tax-exempt parsonage allowance or a tax-exempt military allowance, your expenses for mortgage interest and real estate taxes are deductible under the normal rules. No deduction is allowed for other expenses related to the tax-exempt allowance.

If your housing is provided free of charge and the value of the housing is tax-exempt, you cannot deduct the rental value of any portion of the housing.

Examples of Expenses

Certain expenses are deductible ***whether or not*** you use your home for business. However, if you qualify to claim business use of the home expenses, you can use the business part of these expenses to figure your business use of the home deduction. These expenses include:

- Real estate taxes,
- Deductible mortgage interest, and
- Casualty losses.

Other expenses are deductible ***only*** if you use your home for business. You can use the business part of these expenses to figure your business use of the home deduction. These expenses generally include (but are not limited to):

- Depreciation (covered under *Depreciating Your Home,* later),
- Insurance,
- Rent,
- Repairs,
- Security system, and
- Utilities and services.

Real Estate Taxes

To figure the business part of your real estate taxes, multiply the real estate taxes paid by the percentage of your home used for business.

For more information on the deduction for taxes, get Publication 530, *Tax Information for First-Time Homeowners.*

Deductible Mortgage Interest

To figure the business part of your deductible mortgage interest, multiply this interest by the percentage of your home used in business. You can include interest on a second mortgage in this computation. If your total mortgage debt is more than $1,000,000 or your home equity debt is more than $100,000, your deduction may be limited. For more information on what interest is deductible, get Publication 936, *Home Mortgage Interest Deduction.*

Casualty Losses

If you have a casualty loss on your home that you use in business, treat the casualty loss as a direct expense, an indirect expense, or an unrelated expense, depending on the property affected.

1) Direct expense. If the loss is on the portion of the property you use ***only*** in your business, use the entire loss to figure the business use of the home deduction.
2) Indirect expense. If the loss is on property you use for ***both*** business and personal purposes, use only the business portion to figure the deduction.
3) Unrelated expense. If the loss is on property you ***do not*** use in your business, do not use any of the loss to figure the deduction.

If you are filing Schedule C (Form 1040), get Form 8829 and follow the instructions for casualty losses. If you are an employee or file Schedule F (Form 1040), you can use the worksheet near the end of this publication. You will also need to get Form 4684, *Casualties and Thefts.*

For more information on casualty losses to business and nonbusiness property, get Publication 547, *Casualties, Disasters, and Thefts (Business and Nonbusiness).*

Insurance

You can deduct the cost of insurance that covers the business part of your home. However, if your insurance premium gives you coverage for a period that extends past the end of your tax year, you can deduct only the business percentage of the part of the premium that gives you coverage for your tax year. You can deduct the business percentage of the part that applies to the following year in that year.

Rent

If you rent, rather than own, a home and meet the requirements for business use of the home, you can deduct part of the rent you pay. To figure your deduction, multiply your rent payments by the percentage of your home used for business.

You cannot deduct the fair rental value of your home. If you own your home, see *Depreciating Your Home,* later.

Repairs

The cost of repairs and supplies that relate to your business, including labor (other than your own labor), is a deductible expense. For example, a furnace repair benefits the entire home. If you use 10% of your home for business, you can deduct 10% of the cost of the furnace repair.

Repairs keep your home in good working order over its useful life. Examples of common repairs are patching walls and floors, painting, wallpapering, repairing roofs and gutters, and mending leaks. However, repairs are sometimes treated as a permanent improvement. See *Permanent improvements,* later under *Depreciating Your Home.*

Security System

If you install a security system that protects all the doors and windows in your home, you can deduct the business part of the expenses you incur to maintain and monitor the system. You can also take a depreciation deduction for the part of the cost of the security system relating to the business use of your home.

Utilities and Services

Expenses for utilities and services, such as electricity, gas, trash removal, and cleaning services, are primarily personal expenses. However, if you use part of your home for business, you can deduct the business part of these expenses. Generally, the business percentage for utilities is the same as the percentage of your home used for business.

Telephone. The basic local telephone service charge, including taxes, for the first telephone line into your home is a nondeductible personal expense. However, charges for business long-distance phone calls on that line, as well as the cost of a second line into your home used exclusively for business, are deductible business expenses. You can deduct these expenses even if the expenses for the business use of your home do not qualify for the deduction. Deduct these charges separately on the appropriate schedule. Do not include them in your home office deduction.

Depreciating Your Home

If you own your home and qualify to deduct expenses for its business use, you can claim a deduction for depreciation. Depreciation is an allowance for the wear and tear on the part of your home used for business. You cannot depreciate the cost or value of the land. You recover its cost when you sell or otherwise dispose of the property.

Before you figure your depreciation deduction, you need to know the following information.

- The month and year you started using your home for business.
- The adjusted basis and fair market value of your home at the time you began using it for business.
- The cost of any improvements before and after you began using the property for business.
- The percentage of your home used for business. See *Business Percentage,* earlier.

Adjusted basis defined. The adjusted basis of your home is generally its cost, plus the cost of any permanent improvements that you made to it, minus any casualty losses or depreciation deducted in earlier tax years. For a discussion of adjusted basis, get Publication 551.

Permanent improvements. A permanent improvement increases the value of property, adds to its life, or gives it a new or different use. Examples of improvements are replacing electric wiring or plumbing, adding a new roof or addition, paneling, or remodeling.

If you make repairs as part of an extensive remodeling or restoration of your home, the entire job is an improvement. You must carefully distinguish between repairs and improvements. You must also keep accurate records of these expenses. These records will help you decide whether an expense is a deductible or capital (added to the basis) expense.

Example. You buy an older home and fix up two rooms as a beauty salon. You patch the plaster on the ceilings and walls, paint, repair the floor, install an outside door, and install new wiring, plumbing, and other equipment. Normally, the patching, painting, and floor work are repairs and the other expenses are permanent improvements. However, since the work gives your property a new use, the entire remodeling job is a permanent improvement and its cost is added to the basis of the property. You cannot deduct any portion of it as a repair expense.

Adjusting for depreciation deducted in earlier years. You must decrease the basis of your property by the depreciation you could have deducted on your tax returns under the method of depreciation you properly selected. If you took less depreciation than you could have under the method you selected, decrease the basis by the amount you could have taken under that method.

If you deducted more depreciation than you should have, decrease your basis by the amount you should have deducted, plus the part of the excess deducted that actually decreased your tax liability for any year.

For more information on adjusting your basis for depreciation deducted in earlier years, get Publication 551. If you deducted the incorrect amount of depreciation, see *Incorrect Amount of Depreciation Deducted* in Publication 946.

Fair market value defined. The fair market value of your home is the price at which the property would change hands between a buyer and a seller, neither having to buy or sell, and both having reasonable knowledge of all necessary facts. Sales of similar property, on or about the date you begin using your home for business, may be helpful in figuring the property's fair market value.

Figuring the Depreciation Deduction for the Current Year

If you began using your home for business before 1998, continue to use the same depreciation method you used in past tax years.

If you began using your home for business in 1998, depreciate the business part as nonresidential real property under the modified accelerated cost recovery system (MACRS). Under MACRS, nonresidential real property is depreciated using the straight line method over 39 years. For more information on MACRS and other methods of depreciation, get Publication 946.

To figure the depreciation deduction, you must first figure the part of the cost of your home that can be depreciated (depreciable basis). The depreciable basis is figured by multiplying the percentage of your home used for business by the smaller of:

- The adjusted basis of your home (excluding land) on the date you began using your home for business, or
- The fair market value of your home (excluding land) on the date you began using your home for business.

Depreciation table. If 1998 was the first year you used your home for business, you can figure your 1998 depreciation for the business part of your home by using the appropriate percentage from the following table.

Month of Tax Year First Used for Business	Percentage To Use
1	2.461%
2	2.247%
3	2.033%
4	1.819%
5	1.605%
6	1.391%
7	1.177%
8	0.963%
9	0.749%
10	0.535%
11	0.321%
12	0.107%

Multiply the depreciable basis of the business part of your home by the percentage from the table for the first month in your tax year that you use your home for business. See Table A–7a in Appendix A of Publication 946 for the percentages for the remaining tax years of the recovery period.

Example. In May, George Miller began to use one room in his home exclusively and regularly to meet clients. This room is 8% of the square footage of his home. He bought the home in 1990 for $125,000. He determined from his property tax records that his adjusted basis in the house (exclusive of land) is $115,000. The house had a fair market value of $165,000 in May. He multiplies his adjusted basis (which is less than fair market value) by 8%. The result is $9,200, his depreciable basis for the business part of the house.

George files his return based on the calendar year. May is the 5th month of his tax year. He multiplies his depreciable basis of $9,200 by 1.605% (.01605), the percentage from the table for the 5th month. The result is $147.66, his depreciation deduction.

Depreciating Permanent Improvements

Add the costs of permanent improvements made before you began using your home for business to the basis of your property. Depreciate these costs as part of the cost of the house as explained earlier. The costs of improvements made after you begin using your home for business (that affect the business part of your home, such as a new roof), are depreciated separately. Multiply the cost of the improvement by the business-use percentage and depreciate the result over the appropriate recovery period. For more information on what recovery period to use, see *Property Classes and Recovery Periods* in chapter 3 of Publication 946.

Day-Care Facility

If you use space in your home on a ***regular*** basis for providing day care, you may be able to deduct the business expenses for that part of your home even though you use the same space for nonbusiness purposes. To qualify for this exception to the exclusive use rule, you must meet the following requirements.

1) You must be in the trade or business of providing day care for children, persons 65 or older, or persons who are physically or mentally unable to care for themselves.

2) You must have applied for, been granted, or be exempt from having a license, certification, registration, or approval as a day-care center or as a family or group day-care home under state law. You do not meet this requirement if your application was rejected or your license or other authorization was revoked.

Figuring the deduction. If you regularly use part of your home for day care, figure what part is used for day care, as explained earlier under *Business Percentage.* If you use that part ***exclusively*** for day care, deduct all the allocable expenses, subject to the deduction limit, as explained earlier.

If the use of part of your home as a day-care facility is regular, but ***not*** exclusive, you must figure what part of available time you actually use it for business. A room that is ***available*** for use throughout each business day and that you regularly use in your business is considered to be used for day care throughout each business day. You do not have to keep records to show the specific hours the area was used for business. You may use the area occasionally for personal reasons. However, a room you use only occasionally for business does not qualify for the deduction.

TIP *To find what part of the available time you actually use your home for business, compare the total business-use time to the total time that part of your home can be used for all purposes. You can compare the hours of business use in a week with the number of hours in a week (168). Or you can compare the hours of business use for the tax year with the number of hours in your tax year (8,760 in 1998).*

Example 1. Mary Lake uses her basement to operate a day-care business for children. She figures the business percentage of the basement as follows.

$$\frac{\text{Square footage of the basement}}{\text{Square footage of her home}} = \frac{1,600}{3,200} = 50\%$$

She uses the basement for day care an average of 12 hours a day, 5 days a week, for 50 weeks a year. During the other 12 hours a day, the family can use the basement. She figures the percentage of time the basement is available for use as follows.

$$\frac{\text{Number of hours available for use (12 x 5 x 50)}}{\text{Total number of hours in the year (24 x 365)}} = \frac{3,000}{8,760} = 34.25\%$$

Mary can deduct 34.25% of any ***direct*** expenses for the basement. However, because her ***indirect*** expenses are for the entire house she can deduct only 34.25% of 50% of the indirect expenses. She figures the percentage for her indirect expenses as follows.

Business percentage of the basement	50%
Multiplied by: Percentage of time used	× 34.25%
Equals: Percentage for indirect expenses	17.13%

Therefore, she can deduct 17.13% of her indirect expenses.

Figure B

Form **8829**

Department of the Treasury
Internal Revenue Service

Expenses for Business Use of Your Home

► File only with Schedule C (Form 1040). Use a separate Form 8829 for each home you used for business during the year.

► See separate instructions.

OMB No. 1545-1266

1998

Attachment Sequence No. **66**

Name(s) of proprietor(s): Mary Lake

Your social security number: 412 00 1234

Part I Part of Your Home Used for Business

1	Area used regularly and exclusively for business, regularly for day care, or for storage of inventory or product samples. See instructions	1	1,600
2	Total area of home	2	3,200
3	Divide line 1 by line 2. Enter the result as a percentage	3	50 %
	• **For day-care facilities not used exclusively for business, also complete lines 4–6.**		
	• **All others, skip lines 4–6 and enter the amount from line 3 on line 7.**		
4	Multiply days used for day care during year by hours used per day	4	3,000 hr.
5	Total hours available for use during the year (365 days × 24 hours). See instructions	5	8,760 hr.
6	Divide line 4 by line 5. Enter the result as a decimal amount	6	.3425
7	Business percentage. For day-care facilities not used exclusively for business, multiply line 6 by line 3 (enter the result as a percentage). All others, enter the amount from line 3 ►	7	17.13 %

Part II Figure Your Allowable Deduction

			(a) Direct expenses	(b) Indirect expenses		
8	Enter the amount from Schedule C, line 29, **plus** any net gain or (loss) derived from the business use of your home and shown on Schedule D or Form 4797. If more than one place of business, see instructions				8	25,000
	See instructions for columns (a) and (b) before completing lines 9–20.					
9	Casualty losses. See instructions	9				
10	Deductible mortgage interest. See instructions	10				
11	Real estate taxes. See instructions	11				
12	Add lines 9, 10, and 11	12				
13	Multiply line 12, column (b) by line 7	13				
14	Add line 12, column (a) and line 13				14	-0-
15	Subtract line 14 from line 8. If zero or less, enter -0-				15	25,000
16	Excess mortgage interest. See instructions	16				
17	Insurance	17				
18	Repairs and maintenance	18	171			
19	Utilities	19		850		
20	Other expenses. See instructions	20		8,400		
21	Add lines 16 through 20	21	171	9,250		
22	Multiply line 21, column (b) by line 7	22		1,585		
23	Carryover of operating expenses from 1997 Form 8829, line 41	23				
24	Add line 21 in column (a), line 22, and line 23				24	1,756
25	Allowable operating expenses. Enter the **smaller** of line 15 or line 24				25	1,756
26	Limit on excess casualty losses and depreciation. Subtract line 25 from line 15				26	23,244
27	Excess casualty losses. See instructions	27				
28	Depreciation of your home from Part III below	28				
29	Carryover of excess casualty losses and depreciation from 1997 Form 8829, line 42	29				
30	Add lines 27 through 29				30	-0-
31	Allowable excess casualty losses and depreciation. Enter the **smaller** of line 26 or line 30				31	-0-
32	Add lines 14, 25, and 31				32	1,756
33	Casualty loss portion, if any, from lines 14 and 31. Carry amount to **Form 4684,** Section B				33	-0-
34	Allowable expenses for business use of your home. Subtract line 33 from line 32. Enter here and on Schedule C, line 30. If your home was used for more than one business, see instructions ►				34	1,756

Part III Depreciation of Your Home

35	Enter the **smaller** of your home's adjusted basis or its fair market value. See instructions	35	
36	Value of land included on line 35	36	
37	Basis of building. Subtract line 36 from line 35	37	
38	Business basis of building. Multiply line 37 by line 7	38	
39	Depreciation percentage. See instructions	39	%
40	Depreciation allowable. Multiply line 38 by line 39. Enter here and on line 28 above. See instructions	40	

Part IV Carryover of Unallowed Expenses to 1999

41	Operating expenses. Subtract line 25 from line 24. If less than zero, enter -0-	41	
42	Excess casualty losses and depreciation. Subtract line 31 from line 30. If less than zero, enter -0-	42	

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Mary completes Form 8829 as shown on page 11 (Figure B). In Part I she figures the percentage of her home used for business including the percentage of time the basement is used.

In Part II, Mary figures her deductible expenses. She uses the following information to complete Part II.

Gross income from her day-care business	$50,000
Expenses not related to the business use of the home	$25,000
Tentative profit	$25,000
Rent	$8,400
Utilities	$850
Painting the basement	$500

Mary enters her tentative profit, $25,000, on line 8. (This figure is the same as the amount on line 29 of her Schedule C.)

The expenses she paid for rent and utilities relate to her entire home. Therefore, she enters them in column (b) on the appropriate lines. She adds these two expenses (line 21) and multiplies the total by the percentage on line 7 and enters the result, $1,585, on line 22.

Mary paid $500 to have the basement painted. The painting is a direct expense. However, because she does not use the basement exclusively for day care, she must multiply $500 by the percentage of time the basement is used for day care (34.25% — line 6). She enters $171 (34.25% × $500) on line 18, column (a). She adds lines 21 and 22 and enters $1,756 ($171 + $1,585) on line 24. Because this is less than her deduction limit (line 15), she can deduct the entire amount. She completes the rest of Part II entering $1,756 on line 34. She then carries the $1,756 to line 30 of her Schedule C (not shown).

Example 2. Assume the same facts as in Example 1 except that Mary also has another room that is available each business day for children to take naps in. Although she did not keep a record of the number of hours the room was actually used for naps, it was used for part of each business day. Since the room was available during regular operating hours each business day and was used regularly in the business, it is considered to be used for day care throughout each business day. The basement and room are 60% of the total area of her home. In figuring her expenses, 34.25% of any direct expenses for the basement and room are deductible. In addition, 20.55% (34.25% of 60%) of her indirect expenses are deductible.

Meals. If you provide food for your day-care business, do not include the expense as a cost of using your home for business. Claim it as a separate deduction on your Schedule C (Form 1040). You can never deduct the cost of food consumed by you or your family. You can deduct as a business expense 100% of the cost of food consumed by your day-care recipients and generally only 50% of the cost of food consumed by your employees. However, you can deduct 100% of the cost of food consumed by your employees if its value can be excluded from their wages as a de minimis fringe benefit. For tax years beginning after 1997, the value of meals you provide to employees on your business premises is generally de minimis if more than half of these employees are provided the meals for your convenience. For more information, see chapters 3 and 4 in Publication 535, *Business Expenses.*

If you deduct the cost of food for your day-care business, keep a separate record (with receipts) of your family's food costs.

Reimbursements you receive from a sponsor under the Child and Adult Food Care Program of the Department of Agriculture are taxable only to the extent they exceed your expenses for food for eligible children. If your reimbursements are more than your expenses for food, show the difference as income in Part I of Schedule C. If your food expenses are greater than the reimbursements, show the difference as an expense in Part V of Schedule C. Do not include payments or expenses for your own children if they are eligible for the program. Follow this procedure even if you receive a Form 1099 reporting a payment from the sponsor.

Sale or Exchange of Your Home

If you sold your home after May 6, 1997, you may be able to exclude up to $250,000 ($500,000 for certain married persons filing a joint return) of the gain on the sale. However, you cannot exclude any part of your gain that is equal to any depreciation allowed or allowable for the business use of your home after May 6, 1997.

For more information on the sale or exchange of a home, get Publication 523. If you sold your home before May 7, 1997, see chapter 3 of that publication.

Depreciation. If you used any part of your home for business, you must adjust the basis of your home for any depreciation that was allowable for its business use, even if you did not claim it. If you took less depreciation than you could have under the method you properly selected, you must decrease the basis by the amount you could have taken under that method. For more information, get Publications 551 and 946.

If you used ACRS, MACRS, or some other accelerated method to figure your depreciation, some of the gain on the sale of the business part of your home may have to be treated as ordinary income.

Business Furniture and Equipment

This section discusses the depreciation and section 179 deductions you may be entitled to take for furniture and equipment that you use in your home for business or work as an employee. These deductions are available whether or not you qualify to deduct expenses for the business use of your home.

This section explains the different rules for:

1) Listed property,

2) Property bought for business use, and

3) Personal property converted to business use.

Listed Property

If you use certain types of property, called ***listed property,*** in your home, special rules apply. Listed property includes any property of a type generally used for entertainment, recreation, and amusement (including photographic, phonographic, communication, and video recording equipment). Listed property also includes computers and related equipment unless they are used in a qualifying office in your home. If you use your computer in a qualifying office in your home, see *Property Bought for Business Use,* later. For more information on listed property, see chapter 4 in Publication 946.

More-than-50%-use test. If you bought listed property and placed it in service in 1998, you must use it more than 50% for business (including work as an employee) to claim a section 179 deduction or an accelerated depreciation deduction.

If your business use of listed property is 50% or less, you cannot take a section 179 deduction and you must depreciate the property using the Alternate Depreciation System (ADS) (straight line method). For more information on ADS, see chapter 3 in Publication 946.

Listed property meets the more-than-50%-use test for any tax year if its qualified business use is more than 50% of its total use. You must allocate the use of any item of listed property used for more than one purpose during the tax year among its various uses. You cannot use the percentage of investment use as part of the percentage of qualified business use to meet the more-than-50%-use test. However, you do use the combined total of business and investment use to figure your depreciation deduction for the property.

Example 1. Sarah does not qualify to claim a deduction for the business use of her home, but she uses her home computer 40% of the time for the catering business she operates out of her home. She also uses the computer 50% of the time to manage her investments. Sarah's home computer is listed property because it is not used at a qualified office in her home. Because she does not use the computer more than 50% for business, she cannot elect a section 179 deduction. She can use her combined business/investment use (90%) to figure her depreciation deduction using ADS.

Example 2. If Sarah uses her computer 60% of the time for her catering business and 30% for managing her investments, her computer meets the more-than-50%-use test. She can elect a section 179 deduction. She can use her combined business/investment use (90%) to figure her depreciation deduction using the General Depreciation System (GDS).

Employee. If you use your own listed property (or listed property you rent), in your work as an employee, the property is business-use property only if you meet both of the following requirements.

1) The use is for the convenience of your employer.
2) The use is required as a condition of your employment.

"As a condition of your employment" means that the use of the property is necessary for you to properly perform your work. Whether the use of the property is required for this purpose depends on all the facts and circumstances. Your employer does not have to tell you specifically to have a computer in your home. Nor is a statement by your employer to that effect sufficient.

Years following the year placed in service. If, in a year after you place an item of listed property in service, you fail to meet the more-than-50%-use test for that item of property, you may be required to do both of the following.

1) Figure depreciation, beginning with the year you no longer use the property more than 50% for business, using the straight line method.
2) Figure any excess depreciation and section 179 deduction on the property and add it to:
   a) Your gross income, and
   b) The adjusted basis of your property.

For more information, see *Years After the First Recovery Year* under *Applying the Predominant Use Test* in Publication 946.

Reporting and recordkeeping requirements. If you use listed property in your business, you must file Form 4562 to claim a depreciation or section 179 deduction. Begin with Part V, Section A, of that form.

RECORDS You cannot take any depreciation or section 179 deduction for the use of listed property unless you can prove your business/investment use with adequate records or sufficient evidence to support your own statements.

To meet the adequate records requirement, you must maintain an account book, diary, log, statement of expense, trip sheet, or similar record or other documentary evidence that is sufficient to establish business/investment use. For more information on what records to keep, see *What Records Must Be Kept* in chapter 4 of Publication 946.

Property Bought for Business Use

If you bought certain property to use in your business, you can do any one of the following (subject to the limits discussed later).

- Elect a ***section 179 deduction*** for the full cost of the property.
- Take part of the cost as a ***section 179 deduction*** and ***depreciate*** the balance.
- ***Depreciate*** the full cost of the property.

Section 179 Deduction

You can generally elect to claim the section 179 deduction on depreciable tangible personal property bought for use in the active conduct of your business. You can choose how much (subject to the limit) of the cost you want to deduct under section 179 and how much you want to depreciate. You can spread the section 179 deduction over several items of property in any way you choose as long as the total does not exceed the maximum allowable. You cannot take a section 179 deduction for the basis of the business part of your home.

You elect to take the section 179 deduction by completing Part 1 of Form 4562.

Deduction limits. The section 179 deduction cannot be more than the business cost of the qualifying property. In addition, you must apply the following limits when figuring your section 179 deduction.

1) Maximum dollar limit.
2) Investment limit.
3) Taxable income limit.

Maximum dollar limit. The total cost of section 179 property you can elect to deduct for 1998 cannot be more than $18,500. This maximum dollar limit is reduced if you go over the investment limit (discussed next) in any tax year.

Investment limit. If the cost of your qualifying section 179 property is over $200,000, you must reduce the maximum dollar limit ($18,500) for each dollar over $200,000.

Taxable income limit. The total cost you can deduct each tax year is limited to your total taxable income from the active conduct of all your trade or business activities, including wages, during the tax year. Figure taxable income for this purpose in the usual way, but without regard to all of the following.

1) The section 179 deduction.
2) The self-employment tax deduction.
3) Any net operating loss carryback or carryforward.

For more information on the section 179 deduction, see chapter 2 in Publication 946.

Depreciation

Use Part II of Form 4562 to claim your deduction for depreciation or property placed in service in 1998. It does not include any costs deducted in Part I (section 179 deduction).

Most business property used in a home office is either 5-year or 7-year property under MACRS.

- ***5-year property*** includes computers and peripheral equipment, typewriters, calculators, adding machines, and copiers.
- ***7-year property*** includes office furniture and equipment such as desks, files, and safes.

Under MACRS, you generally use the half-year convention, which allows you to deduct a half year of depreciation in the first year you use the property in your business. If you place more than 40% of your depreciable property in service during the last 3 months of your tax year, you must use the mid-quarter convention instead of the half-year convention.

After you have determined the cost of the depreciable property (minus any section 179 deduction taken on the property) and whether it is 5-year or 7-year property, use the half-year convention table, shown next, to figure your depreciation.

	Percentages	
Recovery Year	**5-Year Property**	**7-Year Property**
1	20%	14.29%
2	32%	24.49%
3	19.2%	17.49%
4	11.52%	12.49%
5	11.52%	8.93%
6	5.76%	8.92%
7		8.93%
8		4.46%

Get Publication 946 for a discussion of the mid-quarter convention and for complete MACRS percentage tables.

Example. During the year, Donald Kent bought a desk and three chairs for use in his office. His total bill for the furniture was $1,975. His taxable business income for the year was $3,000 without any deduction for the office furniture. Donald can elect to do one of the following.

1) Take a section 179 deduction for the full cost of the office furniture.
2) Take part of the cost of the furniture as a section 179 deduction and depreciate the balance.
3) Depreciate the full cost of the office furniture.

The furniture is 7-year property. If Donald does not take a section 179 deduction, he multiplies $1,975, his cost of the furniture, by 14.29% (.1429) to get his depreciation deduction of $282.23.

Personal Property Converted to Business Use

If you use property in your home office that was used previously for personal purposes, you cannot take a section 179 deduction for the property. You can depreciate it, however. The method of depreciation you use depends on when you first used the property for personal purposes.

If you began using the property for personal purposes before 1981 and change it to business use in 1998, depreciate the property by the straight line or declining balance method based on salvage value and useful life.

If you began using the property for personal purposes after 1981 and before 1987 and change it to business use in 1998, you generally depreciate the property under the accelerated cost recovery system (ACRS). However, if the depreciation under ACRS is greater in the first year than the depreciation under MACRS, you must depreciate it under MACRS. For a discussion of depreciation methods for property used for personal purposes before 1987, get Publication 534, *Depreciating Property Placed in Service Before 1987.*

If you began using the property for personal purposes after 1986 and change it to business use in 1998, depreciate the property under MACRS.

The basis for depreciation of property changed from personal to business use is the lesser of:

1) The adjusted basis of the property on the date of change, or

2) The fair market value of the property on the date of change.

Example 1. James Roe bought a desk for $1,000 on November 1, 1986. He began to use it in his home office on February 5, 1998, when it had a fair market value of $600. The depreciable basis of the desk is the fair market value of $600, which is less than its cost. Under ACRS, a desk is 5-year property. Under MACRS, it is 7-year property. Under ACRS, its depreciation is $90 (15%, the first year ACRS percentage for 5-year property, of $600). Under MACRS, its depreciation is $85.74 (14.29%, the first year percentage for 7-year property, of $600). Since the depreciation is greater using ACRS, James must use MACRS to depreciate his desk.

Example 2. Assume the same facts as in Example 1 except that the property is a computer. Under both ACRS and MACRS, a computer is 5-year property. Under ACRS, its depreciation is $90. Under MACRS, its depreciation is $120 (20%, the first year percentage for 5-year property, of $600). Since its depreciation is greater using MACRS, James must use ACRS to depreciate his computer.

Recordkeeping

RECORDS

You do not have to use a particular method of recordkeeping, but you must keep records that provide the information needed to figure your deductions for the business use of your home. You should keep canceled checks, receipts, and other evidence of expenses you paid.

Your records must show the following information.

1) The part of your home you use for business.

2) That you use the part in (1) exclusively and regularly for business as either your principal place of business or as the place where you meet or deal with clients or customers in the normal course of your business (however, see the earlier discussion, *Exceptions to Exclusive Use*).

3) The depreciation and expenses for the business part.

You must keep your records for as long as they are important for any tax law. This is usually the later of the following dates.

1) 3 years from the return due date or the date filed.

2) 2 years from the date the tax was paid.

Keep records to prove your home's depreciable basis. This includes records of your original purchase price, any improvements to your home and any depreciation you are allowed because you maintained an office in your home. You can keep copies of Forms 8829 or the Publication 587 worksheets as records of depreciation.

For more information on recordkeeping, get Publication 583.

Where To Deduct

Deduct expenses for the business use of your home on Form 1040. Where you deduct these expenses on Form 1040 depends on whether you are:

- A self-employed person, or
- An employee.

Self-Employed Persons

If you are self-employed and file Schedule C (Form 1040), attach Form 8829 to your return. If you file Schedule F (Form 1040), report your entire deduction for business use of the home, up to the limit discussed earlier (line 32 if you used the worksheet) on line 34 of Schedule F. Write “Business Use of Home” on the dotted line beside the entry.

Deductible mortgage interest. If you file Schedule C (Form 1040), enter all your deductible mortgage interest on line 10 of Form 8829. After you have figured the business part of the mortgage interest on lines 12 and 13, subtract that amount from the total mortgage interest on line 10. The remainder is deductible on Schedule A (Form 1040), lines 10 and 11. Do not deduct any of the business part on Schedule A. If the interest you deduct on Schedule A for your home mortgage is limited, enter the excess on line 16 of Form 8829.

If you file Schedule F (Form 1040), include the business part of your deductible home mortgage interest with your total business use of the home expenses on line 34. You can use the worksheet near the back of this publication to figure the deductible part of mortgage interest. Enter the nonbusiness part of the deductible mortgage interest on Schedule A (Form 1040), lines 10 and 11.

To determine if the limits on qualified home mortgage interest apply to you, see the instructions for Schedule A (Form 1040) or Publication 936.

Real estate taxes. If you file Schedule C (Form 1040), enter all your deductible real estate taxes on line 11 of Form 8829. After you have figured the business part of your taxes on lines 12 and 13, subtract that amount from your total real estate taxes on line 11. The remainder is deductible on Schedule A (Form 1040), line 6. Do not deduct any of the business part of real estate taxes on Schedule A.

If you file Schedule F (Form 1040), include the business part of real estate taxes with your total business use of the home expenses on line 34. Enter the nonbusiness part of your real estate taxes on line 6 of Schedule A (Form 1040).

Casualty losses. If you are using Form 8829, refer to the specific instructions for lines 9 and 27 and enter the amount from line 33 on line 27 of Form 4684, Section B. Write "See Form 8829" above line 27.

If you file Schedule F (Form 1040), enter the business part of casualty losses (line 31 if you use the worksheet) on line 27 of Form 4684, Section B. Also complete lines 19 through 26 of Section B. Write "See attached statement" above line 27.

Other expenses. Report the other home expenses that would not be allowable if you did not use your home for business (insurance, maintenance, utilities, depreciation, etc.), on the appropriate lines of your Form 8829. If you rent rather than own your home, include the rent you paid on line 20. If any of these expenses exceed the deduction limit, carry them over to next year. They will be subject to the gross income limit from the business use of your home next year.

If you file Schedule F (Form 1040), include your other home expenses that would not be allowable if you did not use your home for business (insurance, maintenance, utilities, depreciation, etc.), with your total business use of the home expenses on line 34 of Schedule F. If any of these expenses exceed the deduction limit, carry them over to the next year. They will be subject to the gross income limit from the business use of your home next year.

Business expenses not for the use of your home. Deduct in full your business expenses that are not for the use of your home itself (dues, salaries, supplies, certain telephone expenses, etc.) on the appropriate lines of Schedule C (Form 1040) or Schedule F (Form 1040). Because these expenses are not for the use of your home, they are not subject to the deduction limit for business use of the home expenses.

Employees

As an employee, you must itemize deductions on Schedule A (Form 1040) to claim expenses for the business use of your home and any other employee business expenses. This generally applies to all employees, including outside salespersons. If you are a statutory employee, use Schedule C (Form 1040) to claim the expenses. Follow the instructions given earlier under *Self-Employed Persons.* The Statutory Employee box within box 15 on your Form W-2 will be checked if you are a statutory employee.

If you have employee expenses for which you were not reimbursed, report them on line 20 of Schedule A. You generally must also complete Form 2106 if:

1) You claim any travel, transportation, meal, or entertainment expenses, or

2) Your employer paid you for any of your job expenses reportable on line 20. (Amounts your employer included in box 1 of your Form W–2 are not considered paid by your employer).

However, you can use a simpler form, Form 2106–EZ, instead of Form 2106, if:

1) You were not reimbursed for your expenses by your employer, or if you were reimbursed, the reimbursement was included in box 1 of your Form W–2, and

2) You use the standard mileage rate if you claim car expenses.

When your employer pays for your expenses, the payments generally should not be on your Form W–2 if you:

1) Are required to account, and do account, to your employer for the expenses, and

2) Are required to return, and do return, any payments not spent for business expenses.

If you account to your employer and your business expenses equal your reimbursement, do not report the reimbursement as income and do not deduct the expenses.

Accounting to employer. You account to your employer when you give your employer documentary evidence and an account book, diary, or similar statement to verify the amount, time, place, and business purpose of each expense. You are also treated as accounting to your employer if your employer gives you a fixed allowance under an accountable plan that is similar in form to an allowance specified by the federal government and you verify the time, place, and business purpose of each expense. For more information, get the instructions for Form 2106 and Publication 463, *Travel, Entertainment, Gift, and Car Expenses.*

Deductible mortgage interest. Although you generally can deduct expenses for the business use of your home on line 20 of Schedule A (Form 1040), do not include any deductible home mortgage interest on that line. Instead, deduct both the business and nonbusiness parts of this interest on line 10 or 11 of Schedule A.

If the home mortgage interest you can deduct on lines 10 or 11 is limited by the home mortgage interest rules, you cannot deduct the excess as an employee business expense on line 20 of Schedule A, even though you use part of your home for business. To determine if the limits on home mortgage interest apply to you, get the instructions for Schedule A or Publication 936.

Real estate taxes. Deduct both the business and nonbusiness parts of your real estate taxes on line 6 of Schedule A. For more information on amounts allowable as a deduction for real estate taxes, get Publication 530, *Tax Information for First-Time Homeowners.*

Casualty losses. Compute the deductible business part of casualty losses in Section B of Form 4684, *Casualties and Thefts.* Enter the business part of casualty losses (line 31 of the worksheet) on line 27 of Form 4684, Section B. Also complete lines 19 through 26. Write "See attached statement" above line 27.

Other expenses. If you file Form 2106 or Form 2106–EZ, report on line 4 the business part of your other expenses (utilities, maintenance, insurance, depreciation, etc.) that do not exceed the deduction limit. Add these to your other employee business expenses and complete the rest of the form. Enter the total from line 10, Form 2106, or line 6, Form 2106–EZ, on line 20 of Schedule A, where it is subject to the 2%-of-adjusted-gross-income limit. If you do not have to file Form 2106 or Form 2106–EZ, enter your total expenses directly on line 20 of Schedule A (Form 1040).

Business expenses not for the use of your home. If you file Form 2106 or Form 2106–EZ, report on line 4 any employee business expenses not related to the use of your home, such as advertising. Enter the total from line 10, Form 2106, or line 6, Form 2106–EZ, on line 20 of Schedule A (Form 1040), where it is subject to the 2%-of-adjusted-gross-income limit. If you do not have to file Form 2106 or Form 2106–EZ, enter these expenses directly on line 20 of Schedule A (Form 1040).

Example. You are an employee who works at home for the convenience of your employer. You meet all the requirements to deduct expenses for the business use of your home. Your employer does not reimburse you for any of your business expenses and you are not otherwise required to file Form 2106 or Form 2106–EZ.

As an employee, you do not have gross receipts, cost of goods sold, etc. You begin with gross income from the business use of your home, which you determine to be $6,000.

The percentage of expenses due to the business use of your home is 20%. The business part of your mortgage interest and real estate taxes is $2,500. Deduct this amount on the lines of your Schedule A (Form 1040) for interest and taxes. Subtract this $2,500 from your gross income from the business use of your home. Your balance is $3,500.

Your total employee business expense related to the business activity in your home, but not due to the use of your home itself, such as advertising, supplies, and telephone use, is $2,000. Subtract this $2,000 from your balance of $3,500. Your other expenses for the business use of your home cannot be more than $1,500.

The business part of your maintenance, insurance, and utilities expense for your home is $800. The business part of your depreciation is $1,600. Add $1,500 ($800 plus $700 of the depreciation expense) to the $2,000 for your other business expenses, and deduct the $3,500 total as a miscellaneous deduction on line 20, Schedule A (Form 1040). It is then included with amounts subject to the 2%-of-adjusted-gross-income limit. Carry over the $900 of your depreciation expense that exceeds the deduction limit to the next tax year, subject to the deduction limit for that year.

Schedule C Example

The filled-in forms for John Stephens that follow show how to report deductions for the business use of your home if you file Schedule C (Form 1040). Only the expenses and information that relate to the business use of the home are discussed.

Form 4562. The following bold line references apply to Form 4562.

Part I, lines 1–13. John began using his home for business in January of this year. He purchased a new computer and filing cabinet to use in his business. The computer, used 100% for business, cost $3,200. The filing cabinet cost $600. He elects to take the section 179 deduction for both items.

John completes Part I of Form 4562. He enters the cost of both the computer and filing cabinet, $3,800, on line 2 and completes lines 4 and 5. On line 6, he enters a description of each item, its cost and the cost he elects to expense. He completes the remaining lines in Part I.

Part II, line 15c. John converted to business use a desk and chair he had purchased in 1992 for personal purposes. In 1992 he paid $1,500 for them. The fair market value in 1998 is $550. Since the fair market value is less than the cost, his depreciable basis is $550.

In Part II, line 15c, column (c), he enters $550 for the desk and chair. He completes columns (d) through (f). Since the furniture is 7-year property under MACRS, he uses the table on page 14 or Table A-1 in Publication 946 to find the rate of 14.29% for property placed in service during the first month of the year. He multiplies $550 by 14.29% (.1429) and enters $79 in column (g).

Part II, line 15i. Because this is the first year John used his home for business, he must figure the depreciation on line 15i. On line 15i, column (c), he enters $11,000, the depreciable basis of the business part of his home. (For a discussion on how the depreciable basis is figured, see *Step 3* under *Form 8829, Part II.)* Because the property is 39-year nonresidential real property under MACRS, he uses the table on page 10 or Table A-7a in Publication 946 to find the rate of 2.461% for property placed in service during the first month of the year. He multiplies $11,000 by 2.461% (.02461) and enters $271 in column (g).

Part IV, line 21. John totals the amounts on line 12 and line 15 in column (g) and enters the total on line 21. He enters both the section 179 deduction ($3,800) and the depreciation on the furniture ($79) on line 13 of Schedule C. He enters the depreciation on his home ($271) on Form 8829, line 28.

Schedule C. The following bold line references apply to Schedule C.

Line 13. John enters the amount from Form 4562 for his section 179 deduction ($3,800) and the depreciation deduction for his office furniture ($79).

Line 16b. This amount is the interest on installment payments for the business assets John uses in his home office.

Line 25. John had a separate telephone line in his home office that he used only for business. He can deduct $347 for the line.

Lines 28-30. On line 28, he totals all his expenses other than those for the business use of his home, and then he subtracts that total from his gross income. He uses the result on line 29 to figure the deduction limit on his expenses for the business use of his home. He enters that amount on line 8 of Form 8829 and then completes the form. He enters the amount of his home office deduction from line 34, Form 8829, on line 30 of Schedule C.

Form 8829, Part I. John uses one room of his home exclusively and regularly to meet clients. In Part I of Form 8829 he shows that, based on the square footage, the room is 10% of his home.

Form 8829, Part II. John uses Part II of Form 8829 to figure his allowable home office deduction.

Step 1. First, he figures the business part of expenses that would be deductible even if he did not use part of his home for business. Because these expenses ($4,500 deductible mortgage interest and $1,000 real estate taxes) relate to his entire home, he enters them in column (b) on lines 10 and 11. He then subtracts the $550 business part of these expenses (line 14) from his tentative business profit (line 8). The result, $25,002 on line 15, is the most he can deduct for his other home office expenses.

Step 2. Next, he figures his deduction for operating expenses. He paid $300 to have his office repainted. He enters this amount on line 18, column (a) because it is a direct expense. All of his other expenses ($400 homeowner's insurance, $1,400 roof repairs, and $1,800 heating and lighting) relate to his entire home. Therefore, he enters them in column (b) on the appropriate lines. He adds the $300 direct expenses (line 21) to the $360 total for indirect expenses (line 22) and enters the total, $660, on line 24. Because this amount is less than his deduction limit, he can deduct it in full. The $24,342 balance of his deduction limit (line 26) is the most he can deduct for depreciation.

Step 3. Next, he figures his allowable depreciation deduction for the business use of his home in Part III of Form 8829. The adjusted basis of his home is $130,000, which is less than the fair market value of $160,000. He figures the value of the land to be $20,000. He subtracts the land value from the adjusted basis. He multiplies the result ($110,000) by the percentage on line 7 to get the depreciable basis of the business part of his home ($11,000).

Because he began using the office in January of this year, it is 39-year nonresidential real property under MACRS. Using the table on page 10 or Table A-7a in Appendix A of Publication 946, he finds that the depreciation percentage for the first year of the recovery period, for assets placed in service in the first month, is 2.461%. His depreciation for 1998 (line 40) is $271 (.02461 × $11,000). He enters that amount in Part II on lines 28 and 30. Because it is less than the available balance of his deduction limit (line 26), he can deduct the full depreciation. (John must also complete Form 4562, see *Form 4562,* earlier.)

Step 4. Finally, he figures his total deduction for his home office by adding together his otherwise deductible expenses (line 14), his operating expenses (line 25), and depreciation (line 31). He enters the result, $1,481, on lines 32 and 34, and on Schedule C, line 30.

SCHEDULE C (Form 1040)

Department of the Treasury
Internal Revenue Service

Profit or Loss From Business

(Sole Proprietorship)

▶ Partnerships, joint ventures, etc., must file Form 1065 or Form 1065-B.

▶ Attach to Form 1040 or Form 1041. ▶ See Instructions for Schedule C (Form 1040).

OMB No. 1545-0074

1998

Attachment Sequence No. **09**

Name of proprietor: John Stephens

Social security number (SSN): 465 00 0001

A Principal business or profession, including product or service (see page C-1): Tax Preparation Services

B Enter NEW code from pages C-8 & 9 ▶ 5 4 1 2 1 3

C Business name. If no separate business name, leave blank.: Stephens Tax Service

D Employer ID number (EIN), if any

E Business address (including suite or room no.) ▶ 821 Union Street
City, town or post office, state, and ZIP code: Hometown, IA 52761

F Accounting method: **(1)** ☒ Cash **(2)** ☐ Accrual **(3)** ☐ Other (specify) ▶

G Did you "materially participate" in the operation of this business during 1998? If "No," see page C-2 for limit on losses ☒ **Yes** ☐ **No**

H If you started or acquired this business during 1998, check here ▶ ☐

Part I Income

1	Gross receipts or sales. **Caution:** *If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see page C-3 and check here* ▶ ☐	1	34,280
2	Returns and allowances	2	– 0 –
3	Subtract line 2 from line 1	3	34,280
4	Cost of goods sold (from line 42 on page 2)	4	– 0 –
5	**Gross profit.** Subtract line 4 from line 3	5	34,280
6	Other income, including Federal and state gasoline or fuel tax credit or refund (see page C-3)	6	– 0 –
7	**Gross income.** Add lines 5 and 6 ▶	7	34,280

Part II Expenses. Enter expenses for business use of your home **only** on line 30.

8	Advertising	8	250	19	Pension and profit-sharing plans	19	
9	Bad debts from sales or services (see page C-3)	9		20	Rent or lease (see page C-5):		
				a	Vehicles, machinery, and equipment	20a	
10	Car and truck expenses (see page C-3)	10	1,266	b	Other business property	20b	
				21	Repairs and maintenance	21	
11	Commissions and fees	11		22	Supplies (not included in Part III)	22	253
12	Depletion	12		23	Taxes and licenses	23	
13	Depreciation and section 179 expense deduction (not included in Part III) (see page C-4)	13	3,879	24	Travel, meals, and entertainment:		
				a	Travel	24a	310
14	Employee benefit programs (other than on line 19)	14		b	Meals and entertainment: 512		
15	Insurance (other than health)	15	750	c	Enter 50% of line 24b subject to limitations (see page C-6): 256		
16	Interest:						
a	Mortgage (paid to banks, etc.)	16a		d	Subtract line 24c from line 24b	24d	256
b	Other	16b	200	25	Utilities	25	347
17	Legal and professional services	17	350	26	Wages (less employment credits)	26	
18	Office expense	18	600	27	Other expenses (from line 48 on page 2)	27	267

28	**Total expenses** before expenses for business use of home. Add lines 8 through 27 in columns ▶	28	8,728
29	Tentative profit (loss). Subtract line 28 from line 7	29	25,552
30	Expenses for business use of your home. Attach **Form 8829**	30	1,481
31	**Net profit or (loss).** Subtract line 30 from line 29. • If a profit, enter on **Form 1040, line 12,** and ALSO on **Schedule SE, line 2** (statutory employees, see page C-6). Estates and trusts, enter on Form 1041, line 3. • If a loss, you MUST go on to line 32.	31	24,071

32 If you have a loss, check the box that describes your investment in this activity (see page C-6).
- If you checked 32a, enter the loss on **Form 1040, line 12,** and ALSO on **Schedule SE, line 2** (statutory employees, see page C-6). Estates and trusts, enter on Form 1041, line 3.
- If you checked 32b, you MUST attach **Form 6198.**

32a ☐ All investment is at risk.
32b ☐ Some investment is not at risk.

For Paperwork Reduction Act Notice, see Form 1040 instructions. Cat. No. 11334P **Schedule C (Form 1040) 1998**

Form **8829**

Department of the Treasury
Internal Revenue Service

Expenses for Business Use of Your Home

► **File only with Schedule C (Form 1040). Use a separate Form 8829 for each home you used for business during the year.**

► **See separate instructions.**

OMB No. 1545-1266

1998

Attachment Sequence No. **66**

Name(s) of proprietor(s): John Stephens

Your social security number: 465 00 0001

Part I Part of Your Home Used for Business

1	Area used regularly and exclusively for business, regularly for day care, or for storage of inventory or product samples. See instructions			1	200
2	Total area of home			2	2,000
3	Divide line 1 by line 2. Enter the result as a percentage			3	10 %
	• **For day-care facilities not used exclusively for business, also complete lines 4–6.**				
	• **All others, skip lines 4–6 and enter the amount from line 3 on line 7.**				
4	Multiply days used for day care during year by hours used per day	4	hr.		
5	Total hours available for use during the year (365 days × 24 hours). See instructions	5	8,760 hr.		
6	Divide line 4 by line 5. Enter the result as a decimal amount	6	.		
7	Business percentage. For day-care facilities not used exclusively for business, multiply line 6 by line 3 (enter the result as a percentage). All others, enter the amount from line 3 ►			7	10 %

Part II Figure Your Allowable Deduction

			(a) Direct expenses	(b) Indirect expenses		
8	Enter the amount from Schedule C, line 29, **plus** any net gain or (loss) derived from the business use of your home and shown on Schedule D or Form 4797. If more than one place of business, see instructions				8	25,552
	See instructions for columns (a) and (b) before completing lines 9–20.					
9	Casualty losses. See instructions	9				
10	Deductible mortgage interest. See instructions	10		4,500		
11	Real estate taxes. See instructions	11		1,000		
12	Add lines 9, 10, and 11	12		5,500		
13	Multiply line 12, column (b) by line 7	13		550		
14	Add line 12, column (a) and line 13				14	550
15	Subtract line 14 from line 8. If zero or less, enter -0-				15	25,002
16	Excess mortgage interest. See instructions	16				
17	Insurance	17		400		
18	Repairs and maintenance	18	300	1,400		
19	Utilities	19		1,800		
20	Other expenses. See instructions	20				
21	Add lines 16 through 20	21	300	3,600		
22	Multiply line 21, column (b) by line 7	22		360		
23	Carryover of operating expenses from 1997 Form 8829, line 41	23		– 0 –		
24	Add line 21 in column (a), line 22, and line 23				24	660
25	Allowable operating expenses. Enter the **smaller** of line 15 or line 24				25	660
26	Limit on excess casualty losses and depreciation. Subtract line 25 from line 15				26	24,342
27	Excess casualty losses. See instructions	27				
28	Depreciation of your home from Part III below	28		271		
29	Carryover of excess casualty losses and depreciation from 1997 Form 8829, line 42	29				
30	Add lines 27 through 29				30	271
31	Allowable excess casualty losses and depreciation. Enter the **smaller** of line 26 or line 30				31	271
32	Add lines 14, 25, and 31				32	1,481
33	Casualty loss portion, if any, from lines 14 and 31. Carry amount to **Form 4684,** Section B				33	
34	Allowable expenses for business use of your home. Subtract line 33 from line 32. Enter here and on Schedule C, line 30. If your home was used for more than one business, see instructions ►				34	1,481

Part III Depreciation of Your Home

35	Enter the **smaller** of your home's adjusted basis or its fair market value. See instructions	35	130,000
36	Value of land included on line 35	36	20,000
37	Basis of building. Subtract line 36 from line 35	37	110,000
38	Business basis of building. Multiply line 37 by line 7	38	11,000
39	Depreciation percentage. See instructions	39	2.461 %
40	Depreciation allowable. Multiply line 38 by line 39. Enter here and on line 28 above. See instructions	40	271

Part IV Carryover of Unallowed Expenses to 1999

41	Operating expenses. Subtract line 25 from line 24. If less than zero, enter -0-	41	
42	Excess casualty losses and depreciation. Subtract line 31 from line 30. If less than zero, enter -0-	42	

For Paperwork Reduction Act Notice, see page 3 of separate instructions. Cat. No. 13232M Form **8829** (1998)

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Form **4562**

Department of the Treasury
Internal Revenue Service

Depreciation and Amortization
(Including Information on Listed Property)

► See separate instructions. ► Attach this form to your return.

OMB No. 1545-0172
1998
Attachment Sequence No. **67**

Name(s) shown on return	Business or activity to which this form relates	Identifying number
John Stephens	Tax Preparations	465-00-0001

Part I **Election To Expense Certain Tangible Property (Section 179) (Note:** *If you have any "listed property," complete Part V before you complete Part I.***)**

1	Maximum dollar limitation. If an enterprise zone business, see page 2 of the instructions	1	$18,500
2	Total cost of section 179 property placed in service. See page 2 of the instructions	2	3,800
3	Threshold cost of section 179 property before reduction in limitation	3	$200,000
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	– 0 –
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see page 2 of the instructions	5	18,500

	(a) Description of property	(b) Cost (business use only)	(c) Elected cost
6	Computer	3,200	3,200
	File Cabinet	600	600
7	Listed property. Enter amount from line 27	7	

8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	3,800
9	Tentative deduction. Enter the smaller of line 5 or line 8	9	3,800
10	Carryover of disallowed deduction from 1997. See page 3 of the instructions	10	– 0 –
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11	18,500
12	Section 179 expense deduction. Add lines 9 and 10, but do not enter more than line 11	12	3,800
13	Carryover of disallowed deduction to 1999. Add lines 9 and 10, less line 12 ► 13 – 0 –		

Note: *Do not use Part II or Part III below for listed property (automobiles, certain other vehicles, cellular telephones, certain computers, or property used for entertainment, recreation, or amusement). Instead, use Part V for listed property.*

Part II **MACRS Depreciation For Assets Placed in Service ONLY During Your 1998 Tax Year (Do Not Include Listed Property.)**

Section A—General Asset Account Election

14 If you are making the election under section 168(i)(4) to group any assets placed in service during the tax year into one or more general asset accounts, check this box. See page 3 of the instructions ► ☐

Section B—General Depreciation System (GDS) (See page 3 of the instructions.)

(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
15a 3-year property						
b 5-year property						
c 7-year property		550	7	HY	200DB	79
d 10-year property						
e 15-year property						
f 20-year property						
g 25-year property			25 yrs.		S/L	
h Residential rental property			27.5 yrs.	MM	S/L	
			27.5 yrs.	MM	S/L	
i Nonresidential real property		11,000	39 yrs.	MM	S/L	271
				MM	S/L	

Section C—Alternative Depreciation System (ADS) (See page 5 of the instructions.)

(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
16a Class life					S/L	
b 12-year			12 yrs.		S/L	
c 40-year			40 yrs.	MM	S/L	

Part III **Other Depreciation (Do Not Include Listed Property.)** (See page 6 of the instructions.)

17	GDS and ADS deductions for assets placed in service in tax years beginning before 1998	17	
18	Property subject to section 168(f)(1) election	18	
19	ACRS and other depreciation	19	

Part IV **Summary** (See page 6 of the instructions.)

20	Listed property. Enter amount from line 26	20	
21	**Total.** Add deductions on line 12, lines 15 and 16 in column (g), and lines 17 through 20. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	21	4,150
22	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	22	

For Paperwork Reduction Act Notice, see the separate instructions. Cat. No. 12906N Form **4562** (1998)

Worksheet To Figure the Deduction for Business Use of Your Home

PART 1—Part of Your Home Used for Business:

1)	Area of home used for business			1) ________
2)	Total area of home			2) ________
3)	Percentage of home used for business (divide line 1 by line 2 and show result as percentage)			3) ________ %

PART 2—Figure Your Allowable Deduction

		(a) Direct Expenses	(b) Indirect Expenses	
4)	Gross income from business (see instructions)			4) ________
5)	Casualty losses	5) ________	________	
6)	Deductible mortgage interest	6) ________	________	
7)	Real estate taxes	7) ________	________	
8)	Total of lines 5 through 7	8) ________	________	
9)	Multiply line 8, column (b), by line 3		9) ________	
10)	Add line 8, column (a), and line 9		10) ________	
11)	Business expenses not from business use of home (see instructions)		11) ________	
12)	Add lines 10 and 11			12) ________
13)	Gross income limit. Subtract line 12 from line 4			13) ________
14)	Excess mortgage interest	14) ________	________	
15)	Insurance	15) ________	________	
16)	Repairs and maintenance	16) ________	________	
17)	Utilities	17) ________	________	
18)	Other expenses	18) ________	________	
19)	Add lines 14 through 18	19) ________	________	
20)	Multiply line 19, column (b) by line 3		20) ________	
21)	Carryover of operating expenses from prior year (see Instructions)		21) ________	
22)	Add line 19, column (a), line 20, and line 21			22) ________
23)	Allowable operating expenses. Enter the **smaller** of line 13 or line 22			23) ________
24)	Limit on excess casualty losses and depreciation. Subtract line 23 from line 13			24) ________
25)	Excess casualty losses (see instructions)		25) ________	
26)	Depreciation of your home from line 38 below		26) ________	
27)	Carryover of excess casualty losses and depreciation from prior year (see instructions)		27) ________	
28)	Add lines 25 through 27			28) ________
29)	Allowable excess casualty losses and depreciation. Enter the **smaller** of line 24 or line 28			29) ________
30)	Add lines 10, 23, and 29			30) ________
31)	Casualty losses included on lines 10 and 29 (see instructions)			31) ________
32)	Allowable expenses for business use of your home. (Subtract line 31 from line 30.) See instructions for where to enter on your return			32) ________

PART 3—Depreciation of Your Home

33)	Smaller of adjusted basis or fair market value of home (see instructions)	33) ________
34)	Basis of land	34) ________
35)	Basis of building (subtract line 34 from line 33)	35) ________
36)	Business basis of building (multiply line 35 by line 3)	36) ________
37)	Depreciation percentage (from applicable table or method)	37) ________
38)	Depreciation allowable (multiply line 36 by line 37)	38) ________

PART 4—Carryover of Unallowed Expenses to Next Year

39)	Operating expenses. Subtract line 23 from line 22. If less than zero, enter -0-	39) ________
40)	Excess casualty losses and depreciation. Subtract line 29 from line 28. If less than zero, enter -0-	40) ________

Instructions for the Worksheet

If you are an employee or file Schedule F (Form 1040), use the preceding worksheet to figure your deduction for the business use of your home. The following instructions explain how to complete each part.

CAUTION *If you file Schedule C (Form 1040), use Form 8829 to figure the deductions and attach the form to your return.*

Part 1—Part of Your Home Used for Business

Lines 1–3. If you figure the percentage based on area, use lines 1 through 3 to figure the business-use percentage. Enter the percentage on line 3.

You can use any other reasonable method that accurately reflects your business-use percentage. If you operate a day-care facility and you meet the exception to the exclusive use test for part or all of the area you use for business, you must figure the business-use percentage for that area as explained under *Day-Care Facility,* earlier. If you use another method to figure your business percentage, skip lines 1 and 2 and enter the percentage on line 3.

Part 2—Figure Your Allowable Deduction

Line 4. If you file Schedule F, enter your total gross income from the business use of your home. This would generally be the amount on line 11 of Schedule F.

If you are an employee, enter your total wages from the business use of the home.

Lines 5–7. Enter your total expenses paid for deductible mortgage interest, real estate taxes, and casualty losses. Under column (a), *Direct Expenses,* enter expenses that benefit only the business part of your home. Under column (b), *Indirect Expenses,* enter expenses that benefit the entire home. You generally enter 100% of the expense. However, if the business percentage of an indirect expense is different from the percentage on line 3, enter only the business part of the expense on the appropriate line in column (a), and leave that line in column (b) blank.

Enter only amounts that would be deductible whether or not you used your home for business. In other words, these amounts would normally be allowable as itemized deductions on Schedule A (Form 1040). Include only the part of a casualty loss that exceeds $100 plus 10% of adjusted gross income.

Lines 9–10. Multiply your total indirect expenses by the business percentage from line 3. Enter the result on line 9. Add this amount to the total direct expenses and enter the total on line 10.

Lines 11–13. Enter any other business expenses that are not attributable to business use of the home on line 11. For employees, examples include travel, supplies, and business telephone expenses. Farmers should generally enter their total farm expenses before deducting office in the home expenses. Do not enter the deduction for half the self-employment tax. Add the expenses on line 11 to the line 10 amount, and enter the total on line 12. Subtract line 12 from line 4, and enter the result on line 13. This is your gross income limit. You use it to determine whether you can deduct this year any of your other expenses for business use of the home. If you cannot, you will carry them over to next year.

If line 13 is zero, deduct your expenses for deductible home mortgage interest, real estate taxes, and casualty losses that would be deductible if you did not use your home for business. Also deduct any business expenses not attributable to use of your home on the appropriate lines of the schedule(s) for Form 1040 as explained earlier under *Where To Deduct.*

Lines 14–21. On lines 14 through 18, enter the total expenses for the business use of your home that would not be allowable if your home were not used for business. These include utilities, insurance, repairs, and maintenance. If you rent, include the amount paid on line 18. If you file Schedule F, include any part of your home mortgage interest that is more than the limits given in Publication 936. (If you are an employee, do not enter any excess home mortgage interest.) In column (a), enter the expenses that benefit only the business part of your home (direct expenses). In column (b), enter the expenses that benefit the entire home (indirect expenses). Multiply line 19, column (b) by the business-use percentage and enter this amount on line 20.

If you claimed a deduction for business use of your home on your 1997 tax return, enter the amount from line 39 of your 1997 worksheet on line 21.

Lines 24–29. On lines 24 through 29, figure your limit on deductions for excess casualty losses and depreciation.

On line 25, figure the excess casualty loss by multiplying the business use percentage from line 3 by the part of casualty losses that would not be allowable if you did not use your home for business ($100 plus 10% of your adjusted gross income).

On line 26, enter the depreciation deduction from Part 3.

On lines 27 through 29, figure your allowable excess casualty losses and depreciation.

If you claimed a deduction for business use of your home on your 1997 tax return, enter on line 27 the amount from line 40 of your 1997 worksheet.

Lines 30–32. On line 30, total all allowable business use of the home deductions.

On line 31, enter the total of the casualty losses shown on lines 10 and 29. Enter the amount from line 31 on line 27 of Form 4684, Section B. See the instructions for Form 4684 for more information on completing that form.

Line 32 is the total (other than casualty losses) allowable as a deduction for business use of your home. If you file Schedule F, enter this amount on line 34 of Schedule F and write “Business Use of Home” on the line beside the entry. Do not add the specific expenses into other line totals of Part II of Schedule F (Form 1040).

If you are an employee, see *Where To Deduct,* earlier, for information on how to claim the deduction.

Part 3—Depreciation of Your Home

Figure your depreciation deduction on lines 33 through 38. On line 33, enter the smaller of the adjusted basis or the fair market value of the property at the time you first used it for business. Do not adjust this amount for changes in basis or value after that date. Allocate the basis between the land and the building on lines 34 and 35. You cannot depreciate any part of the land. On line 37, enter the correct percentage for the current year from the tables in Publication 946. Multiply this percentage by the business basis to get the depreciation deduction. Enter this figure on lines 38 and 26. Complete and attach ***Form 4562*** to your return if this is the first year you used your home, or an improvement or addition to your home, in business.

Part 4—Carryover of Unallowed Expenses to Next Year

Complete these lines to figure the expenses that must be carried forward to next year.

1999 Rules for Business Use of Your Home

New rules, that take effect in 1999, make it easier to claim a deduction for the business use of your home. Under the new rules, you may qualify to claim the deduction, even if you never qualified before.

The following information explains the new rules and gives some examples. If you have a home business, this information will help you plan for your 1999 tax return, which is due April 17, 2000.

CAUTION *The following information does not apply to expenses for the business use of your home in 1998. Those rules can be found at the beginning of this publication.*

Definition of Principal Place of Business for 1999

Beginning in ***1999,*** your home office will qualify as your principal place of business for deducting expenses for its use if:

1) You use it exclusively and regularly for administrative or management activities of your trade or business, and
2) You have no other fixed location where you conduct substantial administrative or management activities of your trade or business.

There are many activities that are administrative or managerial in nature. Some of these activities are:

- Billing customers, clients or patients.
- Keeping books and records.
- Ordering supplies.
- Setting up appointments.
- Forwarding orders or writing reports.

Administrative or management activities performed at other locations. Under the new rules, the following activities will ***not*** disqualify your home office as your principal place of business.

- You have others conduct your administrative or management activities at locations other than your home. (For example, another company does your billing from its place of business.)
- You conduct administrative or management activities at places that are not fixed locations of your business, such as in a car or a hotel room.
- You occasionally conduct minimal administrative or management activities at a fixed location outside your home.
- You conduct substantial nonadministrative or nonmanagement business activities at a fixed location outside your home. (For example, you meet with or provide services to customers, clients, or patients at a fixed location of the business outside your home.)
- You have suitable space to conduct administrative or management activities outside your home, but choose to use your home office for those activities instead.

Other tests. These new rules for “principal place of business” will not affect the other tests you must meet to claim expenses for the business use of your home. You still must use the business part of your home both exclusively and regularly for your trade or business. If you are an employee, the business use of your home must be for the convenience of your employer. In addition, your deduction may be limited if your gross income from the business use of your home is less than your total business expenses. For more information see *Qualifying for a Deduction* and *Deduction Limit,* earlier.

Examples. The following examples describe situations in which an individual's home office will qualify as his or her principal place of business for deducting expenses of its use in 1999, even if the use before 1999 did not qualify. In the following examples, assume the same administrative and managerial activities were conducted in the home office in 1998 and 1999.

Example 1. John is a self-employed plumber. Most of John's time is spent at customers' homes and offices installing and repairing plumbing. He has a small office in his home that he uses exclusively and regularly for the administrative or management details of his business, such as phoning customers, ordering supplies, and keeping his books.

John does not do his own billing. He uses a local bookkeeping service to bill his customers.

In 1998, John's home office did not qualify as his principal place of business because the administrative or management activities, although essential, were considered less important than the work he did in his customers' homes and offices.

Under the new rules, John's home office qualifies as his principal place of business for deducting expenses for its use. He uses the home office for the administrative or managerial activities of his plumbing business and he has no other fixed location where he conducts these administrative or managerial activities. His choice to have his billing done by another company does not disqualify his home office as his principal place of business. Because he meets all of the qualifications, including principal place of business, he can deduct expenses (to the extent of the deduction limit) for the business use of his home in 1999.

Example 2. Pamela is a self-employed sales representative for several different product lines. She has an office in her home that she uses exclusively and regularly to set up appointments and write up orders and other reports for the companies whose products she sells. She occasionally writes up orders and sets up appointments from her hotel room when she is away on business overnight.

Pamela's business is selling products to customers at various locations throughout her territory. To make these sales, she regularly visits customers to explain the available products and take orders.

In 1998, her home office did not qualify as her principal place of business because the essence of her business as a salesperson required her to meet with customers at their places of business. The home office activities were of less importance.

Under the new rules, Pamela's home office qualifies as her principal place of business for deducting expenses for its use. She conducts administrative or management activities there and she has no other fixed location where she conducts administrative or management activities. The fact that she conducts some administrative or management activities in her hotel room (not a fixed location) does not disqualify her home office as her principal place of business. Because she meets all of the qualifications, including principal place of business, she can deduct expenses (to the extent of the deduction limit) for the business use of her home in 1999.

Example 3. Paul is a self-employed anesthesiologist. He spends the majority of his time administering anesthesia and postoperative care in three local hospitals. One of the hospitals provides him with a small shared office where he could conduct administrative or management activities.

Paul does not use the office the hospital provides. He uses a room in his home that he has converted to an office. He uses this room exclusively and regularly to conduct all of the following activities.

- Contact patients, surgeons, and hospitals regarding scheduling.
- Prepare for treatments and presentations.
- Maintain billing records and patient logs.
- Satisfy continuing medical education requirements.
- Read medical journals and books.

In 1998, Paul's home office did not qualify as his principal place of business. The home office activities were less important to Paul's business than the services he performed in the hospitals.

Under the new rules, Paul's home office qualifies as his principal place of business for deducting expenses for its use. He conducts administrative or management activities for his business as an anesthesiologist there and he has no other fixed location where he conducts administrative or management activities for this business. His choice to use his home office instead of one provided by the hospital does not disqualify his home office as his principal place of business. His performance of substantial nonadministrative or nonmanagement activities at fixed locations outside his home also does not disqualify his home office as his principal place of business. Because he meets all of the qualifications, including principal place of business, he can deduct expenses (to the extent of the deduction limit) for the business use of his home in 1999.

Example 4. Kathleen is employed as a teacher. She is required to teach and meet with students at the school and to grade papers and tests. The school provides her with a small office where she can work on her lesson plans, grade papers and tests, and meet with parents and students. The school does not require her to work at home.

Kathleen prefers to use the office she has set up in her home and does not use the one provided by the school. She uses this home office exclusively and regularly for the administrative duties of her teaching job.

In 1998, Kathleen's home office did not qualify as her principal place of business because the administrative activities were less important than her actual teaching duties at the school. Because her home office was not her principal place of business, it was not necessary to determine whether she maintained the office for the convenience of her employer.

In 1999, Kathleen would still have to meet the convenience-of-the-employer test, even if her home qualifies as her principal place of business for deducting expenses for its use. Because her employer provides her with an office and does not require her to work at home, she does not meet the convenience-of-the-employer test and cannot claim a deduction for the business use of her home in 1999.

How To Get More Information

You can order free publications and forms, ask tax questions, and get more information from the IRS in several ways. By selecting the method that is best for you, you will have quick and easy access to tax help.

Free tax services. To find out what services are available, get Publication 910, *Guide to Free Tax Services*. It contains a list of free tax publications and an index of tax topics. It also describes other free tax information services, including tax education and assistance programs and a list of TeleTax topics.

Personal computer. With your personal computer and modem, you can access the IRS on the Internet at ***www.irs.ustreas.gov***. While visiting our Web Site, you can select:

- *Frequently Asked Tax Questions* to find answers to questions you may have.
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- *Forms and Publications* to download forms and publications or search publications by topic or keyword.
- *Comments & Help* to e-mail us with comments about the site or with tax questions.
- *Digital Dispatch* and *IRS Local News Net* to receive our electronic newsletters on hot tax issues and news.

You can also reach us with your computer using any of the following.

- Telnet at **iris.irs.ustreas.gov**
- File Transfer Protocol at **ftp.irs.ustreas.gov**
- Direct dial (by modem) **703–321–8020**

TaxFax Service. Using the phone attached to your fax machine, you can receive forms, instructions, and tax information by calling **703–368–9694.** Follow the directions from the prompts. When you order forms, enter the catalog number for the form you need. The items you request will be faxed to you.

Phone. Many services are available by phone.

- *Ordering forms, instructions, and publications.* Call **1–800–829–3676** to order current and prior year forms, instructions, and publications.
- *Asking tax questions.* Call the IRS with your tax questions at **1–800–829–1040**.
- *TTY/TDD equipment.* If you have access to TTY/TDD equipment, call **1–800–829–4059** to ask tax questions or to order forms and publications.
- *TeleTax topics.* Call **1–800–829–4477** to listen to pre-recorded messages covering various tax topics.

Evaluating the quality of our telephone services. To ensure that IRS representatives give accurate, courteous, and professional answers, we evaluate the quality of our telephone services in several ways.

- A second IRS representative sometimes monitors live telephone calls. That person only evaluates the IRS assistor and does not keep a record of any taxpayer's name or tax identification number.
- We sometimes record telephone calls to evaluate IRS assistors objectively. We hold these recordings no longer than one week and use them only to measure the quality of assistance.
- We value our customers' opinions. Throughout this year, we will be surveying our customers for their opinions on our service.

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CD-ROM. You can order IRS Publication 1796, *Federal Tax Products on CD-ROM,* and obtain:

- Current tax forms, instructions, and publications.
- Prior-year tax forms, instructions, and publications.
- Popular tax forms which may be filled in electronically, printed out for submission, and saved for recordkeeping.
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The CD-ROM can be purchased from National Technical Information Service (NTIS) for $25.00 by calling 1–877–233–6767 or for $18.00 on the Internet at **www.irs.ustreas.gov/cdorders.** The first release is available in mid-December and the final release is available in late January.

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