

Simplifying Home Office Deduction Would Help Small Businesses

The Small Business Advocate, US Small Business Administration, April 2008

In March, the Office of Advocacy published the Top 10 List of Current Rules for Review and Reform. The list was drawn from over 80 rules nominated by small business owners and their representatives in response to Advocacy's Regulatory Review and Reform (r3) initiative.

The need to reform one of these rules—the IRS's home office business deduction—becomes particularly evident in April, as the tax filing deadline is upon us.

Section 280A(c)(1) of the IRS code permits taxpayers to deduct expenses for a home office if it is the principal place of business of the taxpayer, or used exclusively for business, or used to meet with patients, clients, or customers. However, current IRS regulations do not concisely spell out how to qualify for the deduction and how to calculate it. Complicated IRS requirements have evolved instead.

Josh Levine, owner of Electra Entertainment, a home-based business in Ellicott City, Maryland, is very familiar with the home office deduction. "The problem is that many, many self-employed people don't take the home office deduction," Levine explained recently. "They don't understand it; they think that if they take it they're flagging themselves for an audit. And sometimes people take it when they are actually not eligible."

In a recent analysis, Advocacy found that simplifying the home office business deduction would have a significant benefit for small businesses. Home-based businesses make up 53 percent of the nation's small businesses.

Advocacy recommends that the IRS revise its rules to permit a standard deduction for home-based businesses. Similar to the Form 1040 standard deduction, the home office business deduction should be optional. Taxpayers who wish to claim the home office deduction could continue to follow the current home office deduction rules, or choose the new standard deduction.

"This is a huge issue," Levine said. "Obviously when you are self-employed you need as many deductions you can get. The home office is incredibly important since it has an impact on your self-employment tax, which for self-employed individuals is very high."

Only a small percentage of home offices are taking advantage of the deduction. The National Federation of Independent Business estimates that 9 million small businesses have home offices. According to the IRS, however, only 3.2 million tax returns claimed the home office business deduction in 2005.

"Small businesses are entitled to the deduction if they operate from home," Levine said. "And to me, it's very important to be able to take this deduction; it's a huge help."

For questions or concerns about Advocacy's r3 initiative and the home office business deduction, contact Assistant Chief Counsel Dillon Taylor at (202) 401-9787 or [**dillon.taylor@sba.gov**](mailto:dillon.taylor@sba.gov).