

# CLIENT REPORT:

## IRS Tax Tips: Hobbyists

Dear Client:

As part of its Tax Tips series, the IRS has posted information to help taxpayers determine whether their activity is a hobby or a business. Generally, all income must be reported to the IRS. However, if your activity is a hobby, and therefore not carried on for profit, allowable deductions cannot exceed gross receipts for the activity. On the other hand, if your activity qualifies as a trade or business, you may deduct all associated ordinary and necessary expenses.

Here are some factors to consider in determining whether your activity is a hobby or a business:

- Is the purpose of your activity to make a profit? Generally, your activity is considered a business if it is carried on with the reasonable expectation of earning a profit.
- Do you participate in your activity just for fun? Hobbies - also called not-for-profit activities - are those activities that are not pursued for profit.
- Do you depend on income from the activity? Have you changed methods of operation to improve profitability? If the answer to these questions is yes, your hobby may actually be a business.
- Do you have the knowledge needed to carry on the activity as a successful business? People who carry out hobbies just for fun often don't have the business acumen to turn their not-for-profit activity into a profitable business venture.
- Have you made a profit in similar activities in the past? This may indicate your activity is a business rather than a not-for-profit hobby. An activity is presumed carried on for profit if it makes a profit in at least three of the last five tax years, including the current year - or at least two of the last seven years for activities that consist primarily of breeding, showing, training or racing horses.
- Does the activity make a profit in some years? Even if your activity does not make a profit every year, it still may be considered a business.
- Do you expect to make a profit in the future from the appreciation of assets used in the activity? This indicates your activity may be a business rather than a hobby.

We would be happy to review your activity in order to ensure its proper tax treatment. Please call our office at your earliest convenience to arrange an appointment.

Sincerely yours,

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