

Is Your Hobby a For-Profit Activity?

JANUARY 20, 2009

BE IN A POSITION OF STRENGTH

The “hobby loss” rules of IRC Section 183 limit the deduction of expenses from activities that are not engaged in for profit. Under the hobby loss rules, deductions for business type expenses cannot exceed the gross receipts for the activity.

Taxpayers may deduct ordinary and necessary expenses for conducting a trade or business or for the production of income. Trade or business activities and activities engaged in for the production of income are activities engaged in for profit. Presumption of profit intent is created if the activity makes a profit in at least three of the last five years, including the current tax year. There is no negative inference from the failure to meet the presumption test. A taxpayer may establish profit motive even though he fails the test required for the presumption.

Although the determination of intent of the taxpayer is subjective, objective facts are used to determine this intent. No one factor or counting of factors is conclusive, and all facts and circumstances must be taken into account to determine profit motive. The following factors are relevant in determining profit motive:

1. Manner in which the taxpayer carries on the activity
2. Expertise of taxpayers or advisors
3. Time and effort expended by taxpayer in activity
4. Expectation that assets used may appreciate
5. Success of taxpayer in carrying other activities
6. Taxpayer's history of profit or loss with respect to activity
7. Amount of occasional profit earned
8. Financial status of the taxpayer
9. Elements of personal pleasure or recreation

Please contact the tax department to get more details on whether an activity may be affected by the hobby loss rules, and what you should do to avoid a tax challenge.

If you have any questions, please contact the WS+B tax department.

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IS YOUR HOBBY AFFECTED BY THE HOBBY LOSS RULES?

Questions or comments?

E-mail us at taxbriefs@withum.com



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