



HOBBY BUSINESS OR DEDUCTIBLE BUSINESS?

Dear Client:

The current tax law is very specific as to the appropriate guidelines when determining whether an activity is a business or a hobby (an activity not engaged in for profit).

In general, taxpayers may deduct ordinary and necessary expenses for conducting a trade or business. If expenses exceed income, the loss is deductible against other income (such as wages, interest, dividends, etc.) However, if a loss is attributable to an activity not engaged in for profit (hobby), the loss is not allowed as a deduction against other income.

The IRS presumes that an activity is carried on for profit if it is carried on with the reasonable expectation of earning a profit AND if gross income exceeds deductions for three or more out of five consecutive years. If a profit is not made in this timetable, the taxpayer must prove that it is a for-profit business under the facts and circumstances test for it to be characterized as a trade or business.

The tax law provides various penalties that may be imposed to you the taxpayer and us, the preparer, when in audit, and you can not support the basis for your for-profit business.

We therefore are presenting you this other information to consider and answer to help better your position you are asking us to take on your return. We ask you complete this questionnaire, make any comments, and return it to us.

Facts and Circumstances Test

Yes No

- Does the time and effort put into the activity indicate an intention to make a profit?
- Does the taxpayer depend on income from the activity?
- If there are losses, are they due to circumstances beyond the taxpayer's control or did they occur in the start-up phase of the business?
- Has the taxpayer or his/her advisors have the knowledge needed to carry on the activity as successful business?
- Has the taxpayer made a profit in similar activities in the past?
- Does the activity make a profit in some years?
- Can the taxpayer expect to make a profit in the future from the appreciation of assets used in the activity?

Other things to consider determining if a profit motive exists:

- Financial status of taxpayer.
- Elements of personal pleasure or recreation.

Comments: _____

If you feel or it is your position that you have engaged in a for-profit business, please sign and be advised that by signing below:

- You are aware that in the case of an audit, and if you can not satisfy the above tests, penalties and/or the recalculation of income and expenses may be imposed.
- That these preparers have inquired of the above questions and you have proven or provided information necessary to determine that your business is for-profit.
- You are also aware that if for any reason the Internal Revenue Service, the Wisconsin Department of Revenue, any other taxing authority, or any court, shall require you to adjust your tax return in question due to these inclusions, you agree to hold this tax preparer harmless of any tax owed, and any penalties or interest. Further, you agree to pay any additional fees required to amend your return, if required.

 Taxpayer Signature Date

 Taxpayer Signature Date

Tax Return Preparation ■ Financial Statements ■ Payroll Checkwriting ■ Bank Reconciliations ■ Computer Training

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