Forbes

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THE TAX LAWYER

Mar. 8 2012 — 5:46 am

Lawyer's 'International Consulting' A Hobby, Says Tax Court

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Will the IRS pay for your hobby? Not usually. But sometimes yes if you can make it enough of a real business. Kurt Strode should have known this. See *Strode v. Commissioner*. A California attorney, Stode had salary income and tried to offset it by deducting $75,000 a year of expenses from his "international consulting" side business. One problem: In six years, he hadn't made a nickel in international consulting.

Second problem: Strode didn't even show up to Tax Court to explain his business, nor did he send someone who could. That gave the court no choice but to rule for the IRS.

If you want to avoid IRS hassles, my standard advice is to keep business and personal pursuits separate. But many find this a bitter pill to swallow. See Convincing Uncle Sam To Subsidize Your Hobby.

Here are ten tips:

1. **Match income and loss.** The IRS is unlikely to question whether you're engaged in a business if your income from an activity exceeds your expenses.

2. **Keep good records.** It matters whether you conduct yourself in a businesslike manner. Keep good records, hold yourself out as running a business, etc.
3. **Show a profit three years in five.** If you can manage to eke out a profit three years out of every five (or two years out of seven if your activity is horse breeding), the IRS will ***presume*** you're in business to make a profit.
4. **Plan income and expenses**. Our tax system is annual, and so are profit-and-loss determinations. You may have more control than you think over when you receive income and especially when you incur expenses. That control can help you make a profit three years out of five.
5. **Delay a profits determination.** A special tax rule allows you to elect to defer the determination of profit motive until the fourth year of your "business," or sixth year in the case of an activity involving horses. To make this election you file a Form 5213, postponing the determination of whether you've met the three-out-of-five-years profit presumption.
6. **Do it full-time.** The IRS is more likely to go after a taxpayer who writes off his or her "hobby" against other income from a regular job.
7. **Write a business plan**. The IRS looks for businesslike activity. One of the auditors' checklist items is a business plan. Write one up and try to stick to it.
8. **Hire experts and become one.** The more expert you become in a field, and the more you engage other experts, the more business-like you'll look.
9. **Don't enjoy it too much.** Despite societal preoccupation with doing what you love, the IRS looks for elements of personal pleasure or recreation as one indication your "business" is really a hobby.
10. **Combine activities.** If a stand-alone activity produces losses, it may be more at risk of being treated as a hobby by the IRS. If it can be combined with a profitable activity, the IRS might have no problem with it.

For more, see:

Ten Tips For Deducting Your 'Hobby'

Avoid IRS Audit Triggers

The ABCs of Hobby Losses and Profit Motive

When Taxpayers Go Fishing For Deductions

Dr. Faust Goes To Tax Court

Is Your Bathroom Your Home Office?

Taxing Suicide Kits: Business Or Hobby?

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