



Contact:

October 28, 2019

Ryan C. Sheppard, CPA, CFF  
Partner  
Knight Rolleri Sheppard CPAS, LLP  
rcs@krscpasllp.com

**Q: What is the difference between a hobby and a business?**

A: The main difference between a hobby and a business is the profit aspect. The intention of a business is to make a profit while hobbies are engaged in for recreation or pleasure, not for the intention to make a profit.

**Q: How do you determine whether an activity is classified as a hobby?**

A: There is not one factor that will determine whether an activity is a hobby or a business. The IRS has determined the following factors that should be collectively considered to determine whether the activity is a hobby:

1. Is the activity carried in a businesslike manner and maintains a complete and accurate set of books and records?
2. Does the time and effort in the activity indicate the intention to make a profit?
3. Is your livelihood dependent on income from this activity?
4. Are losses in the activity due to circumstances beyond your control?
5. Have you change your method of operation to improve profitability?
6. Do you have the knowledge needed to carry on the activity as a successful business?
7. Were you successful in making a profit in similar activities in the past?
8. Does the activity make profits in some years, how much?
9. Do you expect to make future profits from appreciation of assets used in the activity?

**Q: What is the difference between the tax treatment of a hobby and a business?**

A: A business can deduct expenses that are ordinary and necessary to conduct the activity and any net loss can be deducted against other income. However, for a hobby, losses can only be deducted to the extent of income and are not allowed as a deduction against other income. Prior to 2018, hobby expenses were allowed as 2% itemized deductions. Additionally, taxpayers are not subject to self-employment tax for hobby income.

**Q: What if I want to consider my hobby as a for-profit activity?**

A: With the factors discussed above, the intention to make a profit can be considered in treating the activity as a for-profit business. To incorporate this motive, if profit is established for 3 or more out of 5 consecutive years, the activity is considered a for-profit business (2 out of 7 for horse breeding, training, showing or racing).