

This column features questions from readers submitted via the website. To submit a question to Small Acre Sam, visit BarnyardsandBackyards.com. If your question is featured, you will receive a free one-year subscription to *Barnyards & Backyards!*



ask Sam

question

Dear Sam,

For tax purposes, is my small acreage a hobby or a business?

– Julie, Rawlins

Dear Julie,

Combining business with pleasure? That's great – you should work at what you love. When tax time comes, you may deduct ordinary and necessary expenses for conducting a trade or business or for the production of income. These expenses can offset income generated elsewhere (like from a day job's paycheck). However, people should be careful about incorrectly treating hobby activities as activities engaged in for profit – a problem for which the IRS is on the lookout.

Generally, an activity qualifies as a business if carried on with the reasonable expectation of earning a profit. Here are some questions to ask:

- Does the time and effort put into the activity indicate an intention to make a profit?
- Do you depend on income from the activity?
- If there are losses, are they due to circumstances beyond your control or did they occur in the start-up phase of the business?
- Have you changed methods of operation to improve profitability?
- Do you have the knowledge needed to carry on the activity as a successful business?
- Have you made a profit in similar activities in the past?
- Does the activity make a profit in some years?
- Do you expect to make a profit in the future from the appreciation of assets used in the activity?



The line between hobby and business isn't always clear. Things become more complicated if you have more than one business. A recent court case illustrates this. A Florida woman successfully argued she could deduct losses from her equestrian activities because these were part of a plan to create a profitable interior-design business. The outcome tends to depend on how closely integrated the activities are. In the Florida case, the taxpayer argued her equestrian activities were necessary advertising for her business of designing horse barns and homes – a very close relationship. While she won the case, other cases in which multiple activities were lumped together haven't been successful. So, take note, if there are important connections between your ventures, keep records that can support the correlation between the activities (the "plethora of evidence" was crucial in the Florida case), and put together a compelling business strategy.

If you have a hobby (something that doesn't qualify as a for-profit business), you may still be able to deduct certain items. You would use Schedule A of your Form 1040. For ag business activities, use Schedule F. The IRS website (irs.gov) is worth taking a look at for background. One particular IRS resource is the "Farmer's Tax Guide" (which you can read online or request a hard copy). Another good source for hobby losses, rural ventures, and the Schedule F, is www.ruraltax.org.

— Sam

answer