

Enjoy

Turning a Hobby into a Business

Turning a hobby into a post-retirement business is something many people dream of — and many successful businesses have started out as hobbies. Once a hobby qualifies as a business, favorable tax-deduction rules may apply.

Deducting Expenses

If you operate an active business, business-related expenses generally will be deductible even if they exceed the amount of your business income. Hobby expenses, on the other hand, generally are only deductible up to the amount of income that is generated. They are grouped with any other miscellaneous expenses you have, and only the amount exceeding 2% of your adjusted gross income is deductible.

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IRS Guidelines

The IRS has a set of guidelines to determine whether a hobby qualifies as a business. First and foremost, you must be pursuing the activity with the goal of making a profit. Generally speaking, if you’ve made a profit in three of the last five years, the IRS assumes you intended to make a profit.

If the profit criteria isn’t met, the IRS looks at other factors to determine if a hobby qualifies as a business:

- Do you keep accurate books and records for your venture?
- Do you have checking and credit card accounts for your business (separate from your personal accounts)?
- Do you have special expertise in the venture you’re pursuing?
- Do you spend significant time and effort carrying out the venture?
- Do you reasonably expect that assets used in the venture may appreciate in value?
- Were you financially successful in carrying on other similar or dissimilar ventures?
- Were your business losses attributable to bad luck, illness, or other forces beyond your control?
- Were your occasional profits — if any — significant?
- Does your livelihood depend on the venture’s financial success?



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- Is there little or no personal pleasure or recreation involved in the venture?

If the answer to most of these questions is “yes,” then chances are your venture will be treated as a for-profit activity.

Other Considerations

If you operate your business from home, you may be eligible for a home office tax-deduction. Once again, there are strict IRS guidelines that must be met. In general, you must use your home office

exclusively and regularly as your principal place of business. Your tax adviser can discuss the rules with you in more detail.

Some municipalities have restrictions that apply to home businesses. For example, exterior signs may not be permitted, and regulations may apply if clients visit your home. Insurance is another consideration. If your homeowners insurance does not cover your business assets, you’ll need additional coverage.

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