

Watch the Hobby Farm/Hobby Loss Rules

By Lori Lemmer

Many of our clients ask us questions about starting a farm or business, however, when discussing it with them, many of them are talking about a hobby rather than a real business. For tax purposes, a hobby farm/business has some very unfavorable consequences to the taxpayer. Just a reminder, if it is deemed as a hobby, net income is ALWAYS reported, however, a net loss is NEVER allowed.

Following are some valuable tips to keep in mind and to answer honestly:

- Your intent of the operation is to make money, not create a loss.
- You must run the operation like a regular business. This means having a separate checking account, keeping accurate records, not commingling personal funds or personal expenses, etc.
- If the operation runs at a loss for several years, you must be able to document how it will eventually make money. Generally, 3 out of 5 years must show a profit.
- A horse farm has a greater chance of being determined as a hobby farm.
- The size of the operation can affect the hobby status. It is fairly hard to argue that a 2-acre pasture is a farm.

Remember, the key point to ask yourself: Is this truly an enterprise operated as a business or is it merely intended to create a tax loss? If the latter is true, you may see some IRS red flags.

Thanks,

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