

Business or Hobby

The Internal Revenue Service reminds taxpayers to follow appropriate guidelines when determining whether an activity is a business or a hobby, that is an activity not engaged in for profit. This is an explanation of the rules that determine if an activity qualifies as a business and what limitations apply if the activity is not a business. Incorrect deduction of hobby expenses account for a portion of the overstated adjustments, deductions, exemptions and credits that add up to \$30 billion per year in unpaid taxes, according to IRS estimates. In general, taxpayers may deduct ordinary and necessary expenses for conducting a trade or business. An ordinary expense is an expense that is common and accepted in the taxpayer's trade or business. A necessary expense is one that is appropriate for the business. Generally, an activity qualifies as a business if it is carried on with the reasonable expectation of earning a profit.

In order to make this determination, taxpayers should consider the following factors:

- Does the time and effort put into the activity indicate an intention to make a profit?
- Does the taxpayer depend on income from the activity?
- If there are losses, are they due to circumstances beyond the taxpayer's control or did they occur in the start-up phase of the business?
- Has the taxpayer changed methods of operation to improve profitability?
- Does the taxpayer or his/her advisors have the know-how needed to carry on the activity as a successful business?
- Has the taxpayer made a profit in similar activities in the past?
- Does the activity make a profit in some years?
- Can the taxpayer expect to make a profit in the future from the appreciation of assets used in the activity?

The IRS presumes that an activity is carried on for profit if it makes a profit during at least three of the last five tax years, including the current year – at least two of the last seven years for activities that consist primarily of breeding, showing, training or racing horses. If an activity is not for profit, losses from that activity may not be used to offset other income. An activity produces a loss when related expenses exceed income. The limit on not-for-profit losses applies to individuals, partnerships, estates, trusts, and S corporations. It does not apply to corporations other than S corporations. Deductions for hobby activities are claimed as itemized deductions on Schedule A (Form 1040). These deductions must be taken in the following order and only to the extent stated in each of three categories:

- Deductions that a taxpayer may take for personal as well as business activities, such as home mortgage interest and taxes, may be taken in full.
- Deductions that don't result in an adjustment to basis, such as advertising, insurance premiums and wages, may be taken next, to the extent gross income for the activity is more than the deductions from the first category.
- Business deductions that reduce the basis of property, such as depreciation and amortization, are taken last, but only to the extent gross income for the activity is more than the deductions taken in the first two categories.

Ex. 1 Find the words or expressions in the text which mean the following:

- 1) to figure something out (formally): _____
- 2) to exaggerate the amount of sth: _____
- 3) sth that isn't included: _____
- 4) to point to sth: _____
- 5) a company at an early development stage: _____
- 6) to think that sth is true and correct: _____
- 7) to balance sth: _____
- 8) to list sth: _____
- 9) loss of value: _____
- 10) money paid to workers: _____
- 11) to be more than previously assumed: _____
- 12) expert knowledge: _____

Ex. 2 Match the expressions from the two columns into logical collocations:

- | | |
|---------------------------|---------------------|
| 1) a deduction | year |
| 2) ordinary and necessary | a deduction |
| 3) to depend | premiums |
| 4) circumstances | expenses |
| 5) to improve | profitability |
| 6) a tax | of an expense |
| 7) to produce | an activity |
| 8) to claim | a loss |
| 9) insurance | on sth |
| 10)to carry | beyond sb's control |

Ex. 3 Provide English equivalents of these expressions:

1) kwalifikować się jako	7) kredyt hipoteczny
2) szacunki (założenia)	8) odsetki
3) wzrost wartości aktywów	9) dochód brutto
4) działalność niezarobkowa	10)do poziomu
5) osoba fizyczna	11)zdarzyć się
6) spółka	12)uzasadniony

Grammar corner...

There is a group of verbs in English that are followed either by „to do sth” or by „doing sth”. Here’s a couple of them that go with either that are worth your knowing. With „to do sth”: appear, ask, choose, decide, fail. With „doing sth”: advise, avoid, cease, consider, mention. They are often used in business communication, as you will see below.

Ex. 4 Choose the right option.

- 1) The company appears *to be / being* in good financial situation.
- 2) He was asked *to leave / leaving* due to gross misconduct.
- 3) The CEO advised *to consult / consulting* the legal department on the issue.
- 4) If revenues are as bad as they are now we will cease *to pay / paying* the salaries.
- 5) If you choose *to sell / selling* your stake in the company now, you will lose money.
- 6) We decided *to nominate / nominating* you as the CEO - congratulations!
- 7) The manager avoided *to address / addressing* the issue at the meeting.
- 8) Sadly, we failed *to reach / reaching* agreement, so there’s going to have to be the second round of the negotiations.
- 9) Have you ever considered *to start / starting* your own company?
- 10) He mentioned *to cut costs / cutting costs* during the meeting.

GLOSSARY	
to determine sth	ustalić coś
to overstate sth	podać wyższą wartość niż rzeczywista
an exemption	wyłączenie
to indicate sth	wskazywać na coś
to presume sth	założyć coś (za prawdziwe)
to offset sth	zrównoważyć coś
to itemize sth	wyszczególnić coś
depreciation	utrata wartości
wages	płace
to exceed sth	przekroczyć coś (np. próg dochodu)
a deduction of an expense	odpis wydatku („wrzucenie w koszty”)
circumstances beyond sb’s control	okoliczności posse czyimś wpływem
profitability	dochodowość
to claim a deduction	ubiegać się o odliczenie od podatku
insurance premiums	składki ubezpieczeniowe
to carry on an activity	prowadzić działalność
to qualify as	kwalifikować się jako
estimates	szacunki
appreciation of assets	wzrost wartości aktywów
not-for-profit activity	działalność niezarobkowa
an individual	tu: osoba fizyczna
a mortgage	kredyt hipoteczny
interest	odsetki
gross income	dochód brutto
to the extent	do poziomu
to occur	zdarzyć się
reasonable	uzasadniony
stake in sth	udział w

gross misconduct	rażące przewinienie
due to	z powodu

ANSWER KEY:

Ex. 1

- 1) to determine sth
- 2) to overstate sth
- 3) an exemption
- 4) to indicate sth
- 5) a start-up
- 6) to presume sth
- 7) to offset sth
- 8) to itemize sth
- 9) depreciation
- 10)wages
- 11)to exceed sth
- 12)know-how

Ex. 2

- 1) a deduction of an expense
- 2) ordinary and necessary expenses
- 3) to depend on sth
- 4) circumstances beyond sb's control
- 5) to improve profitability
- 6) a tax year
- 7) to produce a loss
- 8) to claim a deduction
- 9) insurance premiums
- 10)to carry on an activity

Ex. 3

- 1) to qualify as
- 2) estimates
- 3) appreciation of assets
- 4) not-for-profit activity
- 5) an individual
- 6) a partnership
- 7) a mortgage
- 8) interest
- 9) gross income
- 10) to the extent
- 11) to occur
- 12) reasonable

Ex. 4

- 1) to be
- 2) to leave
- 3) consulting
- 4) paying
- 5) to sell
- 6) to nominate
- 7) addressing
- 8) to reach
- 9) starting
- 10) cutting