

Worksheet: Is Your Activity a Business or a Hobby?

This worksheet is designed to help you evaluate your activity's status. The IRS distinguishes between a business (carried on for profit) and a hobby (pursued for sport or recreation). This distinction is critical because it determines how you report income and whether you can deduct your expenses.

Section 1: The IRS Profit Test

The IRS generally presumes an activity is a business if it has been profitable in **three of the last five years** (including 2026).

- **Has your activity earned a net profit in 3 of the last 5 years?**
 - **Yes:** The IRS likely views this as a business.
 - **No:** You must use the 9-factor test below to prove profit motive.

Section 2: The 9-Factor "Profit Motive" Checklist

Review the following questions. A "Yes" answer supports a **Business** classification, while "No" suggests a **Hobby**.

Factor	Checklist Question	Yes	No
1. Manners & Records	Do you keep a separate bank account and formal books (e.g., QuickBooks, spreadsheets)?	<input type="checkbox"/>	<input type="checkbox"/>
2. Expertise	Do you have the necessary knowledge, or do you hire experts to help you succeed?	<input type="checkbox"/>	<input type="checkbox"/>
3. Time & Effort	Do you devote significant time to the activity with the intent to make it profitable?	<input type="checkbox"/>	<input type="checkbox"/>
4. Asset Appreciation	Do you expect the assets you use (equipment, land, etc.) to increase in value?	<input type="checkbox"/>	<input type="checkbox"/>
5. Track Record	Have you successfully turned similar activities into profit-making ventures before?	<input type="checkbox"/>	<input type="checkbox"/>
6. History of Income	Are your current losses due to typical "startup costs" rather than ongoing lack of profit?	<input type="checkbox"/>	<input type="checkbox"/>
7. Occasional Profit	Do you occasionally turn a profit, even if you don't hit the "3-of-5" year rule?	<input type="checkbox"/>	<input type="checkbox"/>
8. Financial Status	Do you rely on this income for your livelihood (not just "extra" money)?	<input type="checkbox"/>	<input type="checkbox"/>

9. Personal Pleasure	Is the activity devoid of significant personal recreation or "fun" elements?	<input type="checkbox"/>	<input type="checkbox"/>
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Section 3: Key Tax Implications for 2026

Feature	Business (Schedule C)	Hobby (Schedule 1)
Income	Report all income.	Report all income.
Expenses	Deduct "ordinary and necessary" costs.	No deductions allowed (since TCJA).
Losses	Can offset other income (W-2, etc.).	Cannot be used to offset income.
Self-Employment Tax	Subject to SE Tax (15.3%).	Not subject to SE Tax.

Section 4: Action Plan & Best Practices

To strengthen your case for a **Business** classification, complete the following:

- Open a Business Account:** If you haven't already, stop mixing personal and business funds.
- Formalize Your Structure:** Consider applying for an EIN.
- Document Your Progress:** Maintain a log of hours worked and a written business plan.
- Review 1099-K Rules:** Be aware that for 2026, payment platforms (Venmo, PayPal) will issue a Form 1099-K if your gross payments exceed \$600.

Disclaimer: This worksheet is for informational purposes only. Tax laws are subject to change. Please consult with our office to review your specific financial situation before filing.