



Robert W. Wood

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Dr. Faust Goes To Tax Court



Image via Wikipedia

While most tax cases may not be interesting to anyone but tax lawyers, some are real [page turners](#). Some offer a glimpse of oddity that downright begs you to say “what were they thinking?” Ronald L. Faust, a retired minister of the [Lake Ozark Christian Church](#), represented himself in [Tax Court](#).

The Tax Court soberly noted that the right Reverend Faust was previously known as Mac Keyes, which was reflected in the name of his new enterprise [MacLeisure Creations](#). It encompassed all he did—so he wrote it *all* off—including:

- Writing books—distributed free to family and friends;
- Buying groceries;
- Buying books and magazines;
- Going on ski trips with friends;
- Buying boating equipment;
- Repairing his washing machine and house;
- Dining out with his wife

- Buying clothing for his son;
- Attending comedy shows and art exhibits; and
- Paying utility and phone bills.

Before you laugh about the chutzpah of claiming such tax deductions, consider that MacLeisure Creations did earn **some** income: a whopping \$210 for 2006. Since the “business” paid out \$36,509 on these important “deductible” items, the 2006 loss was \$36,299. MacLeisure’s results for 2005 were about the same.

The Tax Court applied tried and true tests for discerning what’s a business and what’s a hobby—using a nine-factor test:

1. The manner in which the taxpayer carries on the activity;
2. The expertise of the taxpayer in carrying on the activity;
3. The time and effort expended by the taxpayer in carrying on the activity;
4. The expectation that assets used in the activity may appreciate in value;
5. The success of the taxpayer in carrying on other similar or dissimilar activities;
6. The taxpayer’s history of income or loss with respect to the activity;
7. The amount of occasional profits, if any, which are earned by the taxpayer;
8. The financial status of the taxpayer; and
9. Elements of personal pleasure or recreation.

Reverend Faust had so many problems that it’s hard to critique his tax planning. But as a tax lawyer for the last [30 years](#), what’s the most important way to avoid these hobby loss tax disputes?

Show a Profit Three Years in Five. If you can manage to eke out a profit three years out of every five (or two years out of seven, if your activity is horse breeding), the IRS will **presume** you're in business to make a profit. That presumption is worth a lot since you probably won't have to mud wrestle with the IRS over a more amorphous "facts and circumstances test" that looks at all the details of how you conduct your hobby/business.

If you meet this presumption, the IRS can still argue your activity is not engaged in for profit, but the burden shifts to the IRS. There have been tax cases where taxpayers have beat the IRS in court even though they made a profit only once in 10 or 15 years, but those cases are tough and expensive.

For more, see:

[When Taxpayers Go Fishing For Deductions](#)

[In Pictures: Convincing Uncle Sam To Subsidize Your Hobby](#)

[Ten Tips For Deducting Your 'Hobby'](#)

[What's Your IRS Audit Risk?](#)

[Drag Racing And Amway—Fun Not Profit](#)

[Is Your Hobby A For-Profit Endeavor?](#)

*Robert W. Wood practices law with [Wood LLP](#), in San Francisco. The author of more than 30 books, including *Taxation of Damage Awards & Settlement Payments* (4th Ed. 2009, [Tax Institute](#)), he can be reached at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.*