

BUSINESS PLAN CHECKLIST FOR SECTION 183 ISSUES

The following checklist should be addressed in preparing a **business plan**. Whenever the Internal Revenue Service conducts a tax examination or audit of your individual or business tax return that involves your horse activity, the following areas need to be understood and fully explainable.

I. History of Operation

1. How did it come about?
2. What preliminary investigation was conducted as to demand, profit potential, initial investment, problems, cash flow, market, time period to profit, knowledge required?
3. Why did taxpayer start operation?
4. Intent to show profit - Hobby initially - for how long?
5. What plans does taxpayer have regarding the activity? i.e.: retirement - big profit start small and grow to big business.
6. List sequences of events in activity.

II. Nine Factors under Section 1.183-2(b)(1) to (9):

1. Manner in which the taxpayer carried on the activity.
 - a. Were experts employed?
 - b. Were professionals engaged? I.e.: lawyer, accountant, trainers, and other professionals?
 - c. Formal vs. Informal books - brief description.
 - d. Business checking or co-mingled with personal (did taxpayer keep checks labeled if personal?)
 - e. Was taxpayer involved himself or only passively?
 - f. Overall impression on how taxpayer conducts his business.
 - g. Advertising - how? How often? Where? Is it genuine or not?
 - h. Any leases, contracts, agreements, oral or written?
 - I. Breeding records (stud-sire), winnings.

2. Expertise of Taxpayer or his Advisors:
 - a. Important to know taxpayer's qualifications in the activity.
 - b. What did he do to acquire knowledge and educate him in the activity?
 - c. Advisors consulted - Expertise in field.
 - d. Initially - periodically - special problems - employees (general labor or experts?)
 - e. Were changes made on expert's advice, ignored or implemented?
3. Time and Effort Expended by the Taxpayer in Carrying on This Activity:
 - a. Time taxpayer involved v. time required
 - b. If nominal time, is this adequate; i.e.: Taxpayer hires trainer or ranch to oversee activity.
 - c. What does taxpayer actually do when involved, i.e.: hands on v. observer?
4. Expectation that Assets in the Activity may Appreciate in Value:
 - a. If farming, was land acquired initially for farming? Proof of appreciation rather than guessing!
 - b. Can land be considered part of the activity?
 - c. If horse breeding, proof of horses increasing in value.
 - d. Other assets - why is there expectation of appreciation?
 - e. Is asset necessary for activity?
 - f. Is the appreciation normal or abnormal, i.e.: Did taxpayer buy something specifically for appreciation v. breeding or raising himself?
5. Success of Taxpayer in carrying on other similar and dissimilar activities:
 - a. Was taxpayer previously in this activity? What were the results?
 - b. What other activities has he undertaken? What resulted?
6. Taxpayer's history of income or losses with respect to the activity:
 - a. History of operation, income, losses, type of expenses.
 - b. Can expenses be considered personal?
 - c. Any fortuitous circumstances? Explain consequence.
 - d. Are losses in formidable years normal? For how long?
 - e. Were all years reported as business on Schedule C or F, 1065 or 1120?
7. Amounts of Occasional Profits:
 - a. Why was there a profit? Are all expenses and income reported each year?
 - b. Was there an unusual sale?
 - c. What potential for profit exists and potential recoupment of accumulated losses, including expected gains on the disposition of assets?

8. Financial status of the taxpayer:
 - a. Is he independently wealthy?
 - b. Is he trying to create a tax loss and have Uncle Sam finance his hobby?
 - c. Is he struggling to finance operation?
 - d. For his income, is activity size in proper proportion?

9. Elements of personal pleasure:
 - a. Merely because someone likes his or her work, does not preclude a profit intent.
 - b. How does taxpayer engage in the activity to profit v. personal pleasure?
 - c. If activity involves land, - i.e. ranching, farming, breeding - what recreational amenities are involved? i.e. swimming pool, polo field, training facilities for other than activity necessities, tennis court - how used?
 - d. If horse racing - where raced, how often, who goes, contingency products?
 - e. What assets have both business or personal use - what percentage?
 - f. Identify personal use, amount of time involved, involvement consumption.

III. Three areas within the nine factors should be particularly well developed:

1. What did the taxpayers do to educate themselves about the operation they had undertaken?
2. How accurate, detailed and functional were the records?
3. What did taxpayer do to reduce expenses, minimize loss/maximize profit or cash flow?

I strongly recommend that you talk with your tax advisor or accountant if you do not understand this area. Specific questions can be addressed to Patrick J. Hurley at (800) 996-1040.