

# Tips For Doing Your Taxes

## Is your art a business?

- **A little bit about Schedule C and sole-proprietorships...**
  - One of the defining characteristics of a sole proprietorship is that there is no legal difference between you and your business. Therefore, it is up to you to establish a clear separation between your personal and business expenses.
  - Schedule C is part of your individual tax return (1040) and is required for a sole-proprietorship business.
  - A loss reported on a Schedule C is one of the most common triggers for an IRS audit. Therefore, it is important to keep accurate records of your business expenses.
  
- **The IRS looks at nine criteria to help determine if a business is actually a business and not a hobby. Please note: these criteria are only guidelines and are not intended to secure a tax position.**
  1. Do you carry on in a businesslike manner? Letterhead, business cards, prospecting efforts, etc.
  2. Do you spend sufficient time and effort in the activity? Document how much time you spend on your art, including conferences, classes, etc.
  3. Are you depending on income from your art for your livelihood?
  4. Are losses due to startup costs or circumstances beyond your control?
  5. Do you change your methods in an effort to improve your profitability?
  6. Do you have sufficient knowledge to be successful? Continuing education, keep up with the times, etc.
  7. Have you been successful at similar activities in the past?
  8. Do you make a profit in some years and how large is the profit? Some large art projects may take over a year to complete.
  9. Do you expect to make a profit from appreciated assets?
  - Use the 3 out of 5 year test: Did you make a profit 3 out of the past 5 years?
  - What constitutes income?
    - Cash or other consideration received in exchange for your art.
    - If you exchange artwork with another artist, you receive artwork at retail value, but give artwork at your cost.
  - You can only account for hard costs.
    - Your time is not a hard cost, so you cannot deduct it.
    - If someone steals your art or you sell your artwork and never collect the cash, you have only lost the money that went into making the art (i.e. materials costs), not the retail value.
    - If you donate a painting, you can only take a deduction for the cost of your materials, not the retail price of the work.

*Please note: This handout was created by Visual Art Exchange based on a lecture by Alex Lehmann on 10.22.2009 at Meredith College as part of VAE's Business of Being an Artist Lecture Series. These notes are guidelines for artists and are not intended to be tax or legal advice. Please contact your tax advisor with specific tax questions.*

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## Possible Allowable Business Deductions for Visual Artists

- **All deductions depend on facts and circumstances.**
  - All deductions must be for business purposes.
  
- **The Shoebox Accounting Method**
  - What to put in the box:
    - Business bank account statements
    - Business credit card statements
    - Cancelled checks
    - Sales invoices
    - Mileage logs
    - Commissions paid
    - Receipts for:
      - Supplies
      - Meals & entertainment
      - Airfare & hotels
      - Parking & taxicabs
      - Auto repairs
      - Gasoline
      - Equipment purchased
  - Give the shoebox to your accountant to figure out your deductions.
  
- **Possible deductions in greater detail...**
  - **TRAVEL**
    - The IRS does not have a set number of miles away from home to determine whether travel expenses are warranted. 50-100 is a recommended minimum.
    - Commuting miles are not business miles.
    - Mixed-use trips: The trip must be primarily for business purposes. Even then, only days for which the primary purpose is business can expenses be deducted.
  - **AUTO/VEHICLE**
    - It is sometimes difficult to keep track of actual expenses, so many people deduct mileage.
    - The mileage deduction for 2009 is 55¢ per mile and 50¢ per mile for 2010.
    - Keep a mileage log and/or a travel calendar so you can calculate mileage. For instance, if you know you traveled from your home in Raleigh to the McColl Center in Charlotte, you can use Google Maps to calculate the distance traveled.

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- **MEALS**
  - There is a difference between actual meal costs & a meal allowance. A meal allowance is a set amount based on the cost of living in the area you are visiting.
  - If you take someone out to a business lunch, keep the person's business card, write the date & time on the back of the card, staple to meal receipt and put it in your shoebox.
- **HOME STUDIO**
  - Must be exclusively for business use. Most people fail the exclusive-use test during an audit.
  - If you have a computer in your home studio, use that computer exclusively for business. (no personal email, kids' homework, etc.)
  - Calculate the square footage of your studio divided by the total square footage of your home to determine the percentage of common expenses you may deduct as business expenses (rent, insurance, etc.).

## **Banking & Bookkeeping**

- **It is recommended to keep a separate bank account for your business.**
  - Helps support that your business is actually a business, not a hobby.
  - It can be a personal-type bank account.
  - Helps keeping track of your business expenses.
  - You can "lend to yourself" by transferring money from your personal account to your business account and paying yourself back later.
  - A good way to substantiate your business expenses is with a check from your business account, rather than cash or debit card. Receipts are often lost or misplaced, while a copy of a check can always be retrieved from the bank.
  - Bank statement entries can substitute for a receipt in some cases, but it is always better to have a receipt.
- **Use an electronic record keeper, like Quickbooks.**
  - These programs are designed for non-accountants and easy to use. They are also inexpensive for a basic version (\$20-50).
  - You can often buy an older version of the software at a discount through an online retailer.

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