

Tax Time for Photographers **Text copyright Heather Forcier, all rights reserved**

Many photographers in the United States find themselves confused at tax time regarding their federal and state reporting obligations. There is no substitute for consulting with an accountant and lawyer regarding your business concerns. However, it does help to be informed in preparation for these meetings to make the most of your time.

ARE YOUR PHOTOGRAPHY ACTIVITIES A BUSINESS OR A HOBBY?

According to the IRS, "A trade or business is generally carried on to make a profit." (Pub. 334) Carefully consider if you truly intend your income from photographic activities to cover your related expenses, including gear, photo trips, and other incidental expenses. It may take several years before you are able to meet such a goal, but do you have this profit motive?

Nature photography can be a particularly difficult business during start up due to the often-substantial investment in equipment plus the number of years it takes to build a viable portfolio and start making appropriate contacts for sales.

If you don't really expect that your photographic earnings will ever cover the constant gear upgrades and the tours to various destinations, your activities may be a "hobby" by the IRS definition. A hobby is "an activity from which you do not expect to make a profit." (IRS website, "Is it a Business or a Hobby?")

The IRS offers a number of factors for consideration to determine if your activity is for profit. The more of these that can be met, the better. (IRS website, "Is it a Business or a Hobby?")

1. You carry on the activity in a business-like manner,
2. The time and effort you put into the activity indicate you intend to make it profitable,
3. You depend on income from the activity for your livelihood,
4. Your losses are due to circumstances beyond your control (or are normal in the start-up phase of your type of business),
5. You change your methods of operation in an attempt to improve profitability,
6. You, or your advisors, have the knowledge needed to carry on the activity as a successful business,
7. You were successful in making a profit in similar activities in the past,
8. The activity makes a profit in some years and the amount of profit it makes, and
9. You can expect to make a future profit from the appreciation of the assets used in the activity.

PROFIT MOTIVE

You are presumed to have a profit motive if your activities have shown a profit in three of the last five years, including the current year. Failure in meeting this profit test doesn't necessarily mean you will be reclassified as a hobby. At the same time, success in meeting this profit test doesn't necessarily mean you cannot be reclassified as a hobby, either. Review the factors the IRS considers and ensure your commitment to photography is consistent with a viable business to improve your chances of keeping a business status.

What does the business-versus-hobby classification ultimately mean for you? A business can generally deduct most of its ordinary and necessary expenditures. With a hobby, there is a limit to the deductions you can take; they are usually capped at the extent of your income related to the endeavor. For example, if you spent \$4,000 during the year on your photography but only earned \$300, it is unlikely you will be able to deduct more than \$300 worth of your expenses.

While it would be advantageous to deduct all of your costs in photography, doing so and filing years of constant losses may be a flag to the IRS. If your status as a business truly seeking a profit comes into question, your returns may be analyzed further, and the possibility exists that the IRS may disagree with your profit motive. This could mean reclassification as a hobby retroactively, with recalculations creating taxes due from prior years, including the possibility of interest and penalties.

BUSINESS ENTITY

Regardless of your business or hobby classification, income related to your photographic endeavors will be considered reportable income.

If your activity has been deemed a hobby, the proper form for reporting the income is Form 1040: U.S. Individual Income Tax Return, typically on the last line of the income section under "other income." Expenses may be reported on Schedule A: Itemized Deductions, which is attached to the Form 1040. Hobby expenses are "Miscellaneous Itemized deductions (Subject to 2% of your income)," meaning in many cases that you might not actually get a deduction unless your total miscellaneous itemized deductions exceed 2% of your adjusted gross income (AGI).

If you have a photography business, consider how you started. If you simply purchased some equipment, started taking photos and selling your work without working with a lawyer or accountant to create a specific business entity, it is likely you are a "sole proprietor." Sole proprietors report income and expenses on Schedule C: Profit or Loss from Business. Other business entities include limited liability companies (LLC), partnerships, and corporations. Consult with your accountant and lawyer regarding the tax and legal advantages of these other business forms for you.

STATE OBLIGATIONS

Whether your photography is a business or a hobby, you may have reporting obligations to your state. Each state is different; next to consulting with a local accountant you can contact your state business tax department for a packet of information.

A common obligation for photographers selling their work as prints is state sales tax, where the state tax rate is assessed on the purchase price, collected by the photographer, then reported and remitted to the state on a periodic basis. Registering for a sales tax identification number may have its benefits: in some states certain purchases may be made tax exempt by providing a copy of your certificate.

RECORDKEEPING

Keeping hundreds of receipts of varying sizes in order is never an easy task. Try to develop a good system and keep it up to date. If photography is a business for you, consider investing in an accounting program like Quickbooks, which is quite popular and doesn't require an accounting degree to understand and use.

INCOME

According to the IRS, "Except as otherwise provided in the Internal Revenue Code, gross income includes income from whatever source derived." (2005 Instructions for Schedule C) It's a good idea to create different accounts in your accounting program to keep track of different types of income, such as print sales, editorial sales, advertising usage, etc. Create a miscellaneous income account for those payments you have a hard time classifying, and at the end of the year print out the detail for that account to provide to your accountant who can review and classify the items for you. For example, if you sell some of your equipment, unless you fully understand how this type of information gets reported for tax purposes, it might be best to put the gross proceeds from the sale in the miscellaneous income account for the accountant to sort out later.

EXPENSES

According to the IRS, business expenses must be "ordinary and necessary" to be deductible, essentially expenditures that are "common and accepted" in your line of business, as well as "helpful and appropriate" in your endeavors. (Pub 334)

Capital Purchases

What can get confusing is payments that are considered "capital purchases." These types of expenses are for assets like your camera gear, computer equipment, and other property acquired that has a "useful life that extends substantially beyond the year it is placed in service." (Pub 334) For example, your camera gear should realistically be usable for a number of years, regardless of whether or not you upgrade camera bodies frequently.

Capital items are not expensed in the year purchased, but are instead depreciated according to an estimated useful life set forth by the IRS so that the depreciation expense is taken over that period of time. There are different lives for different groups of assets, and numerous depreciation methods. Under certain circumstances, your asset purchases may be eligible for §179 expense, whereby you can expense the entire amount of your capital purchase(s) in the current year, with limitations.

Note that it is customary to have a reasonable "capitalization policy," where a business determines, based on its size and its asset purchases, what purchase price for a single item will be considered a capital purchase. A small sole proprietorship might have a capitalization policy of \$100 or \$150, because it would be cumbersome to maintain records on lots of little items less than that dollar amount. For example, you would expect a CompactFlash card reader you purchased for \$50 would last for years, but keeping track of lots of low dollar items on a depreciation schedule would be a great deal of recordkeeping. While pens and other small supplies might last for years, they are generally considered an "office supplies" expense.

When you purchase an asset, also consider your business versus personal use of it. For example, your purchase of a 600mm lens is likely to be used solely in the pursuit of wildlife images related to your photography business, and unlikely to be used

for personal reasons. But if you buy a computer, how much of the use is truly business-related and how much is personal? Consider these questions in preparation for the meeting with your accountant.

Travel

Part of your nature photography might take place in your backyard, but chances are good that you have to travel sometimes as well. Keep track of your travel receipts and discuss these activities with your accountant to see what you can get deductions for. When traveling in your own vehicle, you may be able to get a deduction at the “standard mileage” rate, so it is in your best interest to record the miles you drive for photography by noting the dates, starting and ending odometer readings, and the trip it relates to.

Upon speaking with your accountant, you may find that the cost of your meals are deductible, but don't be surprised when you find out you are disallowed half of the expense. Eligible meals costs are only deductible at 50% of what you paid.

Business travel that requires you be away overnight means you may be able to use the federal per diem rate for meals, which can be easier than collecting all of the receipts from your actual meal expenses. The per diem rates are published on the IRS website and vary by location. Note that these rates are also reduced by 50% on your tax return.

Business Use of Your Home

If you have a photography business, chances are good you do your editing and image processing in your home, and likely conduct most of your administrative duties such as recordkeeping at home. To deduct any expenses for the use of your home in business, you must meet specific guidelines set forth by the IRS. As a nature photographer, your home is likely the principal place where you conduct businesses and you use it regularly for this purpose, which is one test. A more difficult test to meet is “exclusive use,” meaning “you must use a specific area of your home only for your trade or business.” “You do not meet the requirements of the exclusive use test if you use the area in question for both business and personal purposes.” (Pub 334) Consult with your accountant regarding your business use of your home to see what deductions you might be eligible for.

FREQUENTLY ASKED QUESTIONS

Q: What deduction can I get if I contribute a print to a charity?

A: If you have a photography business and are already deducting your supplies – the paper and ink it took to make that print – you have already deducted all that you can. If your photographic endeavors are considered a hobby, keep track of the costs of any donated items and present that information to your accountant at year end.

Q: What is the difference between “cash basis” and “accrual basis” accounting?

A: Simply put, cash basis accounting means a business doesn't show income until payments are received and doesn't show expenses until they are paid. Note that credit card purchases can be treated as current expenses, even if you haven't paid the credit card bill yet. Accrual basis means that income and expenses are “matched” in the period in which they were earned or incurred. For instance, if you bill a client for \$2,000 on December 30, 2005, but don't receive the check until January 16, 2006, the income would be reported for 2005.

Generally, small businesses use the cash method of accounting, but consult with your accountant about your situation to see which method is best for you. If you have inventory, you may have to use the accrual basis for your inventory transactions, but may be able to use cash basis accounting for all other transactions. For example, if you have prints in a gallery for sale, accrual basis accounting for this inventory means you cannot deduct the cost of the prints, mats, frames, and glass until the print actually sold.

Q: What are self-employment taxes and do I have to pay them?

A: Self-employment tax is the way a self-employed individual remits their Social Security and Medicare taxes. Generally, you will be subject to self-employment taxes if your net earnings are \$400 or more.

Q: My client wants my tax ID number, or I have received a 1099-MISC from a client. What does this mean?

A: The IRS requires that certain payments be reported regarding independent contractors, much like receiving a W-2 from an employer. A client may need your tax identification number, usually your Social Security Number unless you have filed for a separate Employer Identification Number, for these reporting purposes. You can use IRS Form W-9 to provide your tax ID to your client, which may be used when the client prepares a 1099-MISC for their payments to you during the year.

One part of the 1099-MISC form gets reported to the IRS, so they know you have received income. Keep track of all of the 1099-MISC forms you receive from clients and use them to check the gross revenues you report, which in total should meet or exceed the total of the income reported to you on the 1099-MISC forms. Note that since the IRS has received this information,

it is likely they are comparing the numbers too, so if there are any discrepancies be sure your accountant understands them so they can be reported appropriately.

Q: I gave someone one of my prints in exchange for something else I wanted. No money changed hands, do I have to report this?

A: What has occurred in this situation is a barter transaction. If you have exchanged your photo for something you will be using in your business, the net effect is a “wash,” as your income matches your expense exactly. But for proper recordkeeping, a reasonable value should be assigned to the items, which would be the same amount since they were exchanged, and recorded as a transaction in your books.

However, if you exchanged it for a non-business item, then you have income but no expense, and the income should be reported.

IN SUMMARY

Hopefully this information has been helpful to you in preparing for a meeting with your accountant – the single best resource you have. Here are a few other resources you may find helpful:

Photoattorney.com - The website of photographer and attorney Carolyn E. Wright, with lots of great information for photographers.

[J.K. Lasser's Your Income Tax](#) - J.K. Lasser provides a thorough tax guide each year which is very well written and easy to follow. (Click on the link to get the guide from Amazon.com or visit your local bookstore.)

The www.irs.gov website - Look up forms and publications in PDF format. Publication 334: Tax Guide for Small Business is a great starting reference.



Disclaimer: This article is for informational purposes only; it may be out of date, incomplete or incorrect. It is not intended to constitute accounting or tax advice nor does it intend to replace or establish a professional accounting relationship. Please consult with an accountant regarding your personal accounting and tax situation.

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Feel free to send your comments on this article to the [editors](#) at NatureScapes.Net.

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