



Fact Sheet

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Reporting Auction Income and the Tax Gap

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Many people don't realize the income they earn from auctions and consignment sales may be taxable. This fact sheet, the 16th in the Tax Gap series, will help taxpayers better understand what income they are required to report and what deductions they may be entitled to take.

The tax gap, or the amount of tax that goes unpaid each year, results from taxpayers underreporting their taxable income. Fortunately most people want to pay their fair share of taxes and many simply need a better understanding of their obligations.

What's Taxable

All income from auctions, traditional or online, and consignment sales is generally taxable unless certain exceptions are met. This income is usually considered either "business" or "ordinary" income. In certain circumstances such income can qualify for capital gain treatment. There are also some exceptions where income can be excluded from taxable income.

Business income resulting from an auction or consignment sale is subject to the same taxes as the income of any other retail or service business. That may include [income tax](#), [self-employment tax](#), [employment tax](#), or [excise tax](#). A retail or service business owner must include this income in his or her business income.

A person must report a gain from a sale whether he or she operates a business or not. A reportable gain is the income above the original cost or basis of the item. These gains may be [business income](#) or [capital gains](#).

Income resulting from auctions akin to an occasional garage or yard sale is generally not required to be reported. However, there may be exceptions. If an online garage sale turns into a business with recurring sales and purchasing of items for resale, it may be considered an online auction business.

Some people sell a product or service online as a hobby. This income generally must be reported and deductible expenses are limited. The deductions cannot total more than the income reported and can only be taken if deductions are itemized on [Form 1040, Schedule A, Itemized Deductions](#).

For additional information about whether an activity is a business or a hobby, see April's fact sheet titled, [Business or Hobby? Answer Has Implications for Deductions](#).

What's a Deductible Expense

Traditional or online auction and consignment sellers in the business to make a profit can generally deduct expenses that are both ordinary and necessary. An "ordinary" expense is one that is common and accepted in a trade or business. A "necessary" expense is one that is helpful and appropriate for a trade or business. Verifiable auction and consignment fees and commissions are examples of allowable business expenses.

Expenses related to personal, living, or family matters are generally not deductible. There are expenses that are partly personal and partly business-related. The business portion of the expense is deductible.

Here's a simple example. A person might borrow \$10,000, using \$7,000 for personal use and the other \$3,000 for his or her online auction business. The interest expense on the \$7,000 is not deductible but the interest on the other \$3,000 is deductible. Chapter 5 of [Publication 535, Business Expenses](#) can help a taxpayer understand these rules better.

A common split expense issue is a person's home that they also use for their business. That person may be able to deduct expenses for the business use of the home if they meet the regular use requirement and the exclusive use requirement.

However, auction and consignment sellers may compute their deduction to the extent of expenses allocable to space in the residence that is used on a regular basis (does not have to be exclusive) to store inventory and/or product samples if the residence is the sole fixed location of the retail or wholesale auction or consignment business.

Allocable expenses may include mortgage interest, insurance, utilities, repairs, and depreciation. Refer to [Publication 587, Business Use of Your Home](#) for more information.

Additional information about [business expenses](#), [starting](#) and [operating](#) a business, and [online auction sellers](#) is available at www.irs.gov.