

# THE FREELANCER'S TAX GUIDE

NAVIGATING THE SELF-EMPLOYED TAX PUZZLE

Nothing strikes fear into the heart of a freelancer like the mention of end-of-the-year taxes. It's a difficult puzzle for the self-employed (as if the tax system wasn't complicated enough); and, unless you fit the pieces together perfectly you'll end up paying some hefty fines. Need help? Use this tax guide to get you safely through the season.

## TAX OBLIGATIONS FOR FREELANCERS

Unlike W-2 employees, freelancers have to cover their own payroll taxes and an additional self-employment tax. Below are some of your potential tax obligations as a freelancer.

### 1 SELF-EMPLOYMENT TAX

SE tax is a Social Security and Medicare tax primarily for individuals who work for themselves.

### 2 INCOME TAX

An income tax is a tax levied on the income of individuals or businesses (corporations or legal entities).

### 3 QUARTERLY TAXES

Quarterly taxes are the method used to pay tax on income that is not subject to withholding.

#### SELF-EMPLOYMENT TAX

##### DO YOU QUALIFY?

Almost all freelancers are subject to the self-employment tax if they meet these requirements:

##### HOW MUCH WILL YOU OWE?

In 2010, the self-employment tax rate was 15.3%. But in 2011, due to the 2011 Tax Relief Act, the rate will be 13.3%.

#### QUALIFICATIONS

1 Your net earnings must be greater than \$400 (excluding church employee income).



#### 2

You are a church employee with income greater than \$108.28.



#### RATES



For both 2010 and 2011, any income earned after the first \$106,800 is not subject to the social security tax.

#### QUARTERLY TAXES

##### WHY PAY QUARTERLY?

You can pay your taxes either quarterly or monthly. You can also wait and pay all your taxes at the end of the year, if you are prepared to incur some hefty fines and a possible audit.

#### PAYMENT DATES

If you choose to pay quarterly, there are dates set forth by the IRS that are quarterly payment deadlines.

APRIL 15TH	JUNE 15TH	SEPT. 15TH	JAN. 15TH
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January 15th after the end of your tax year.

##### DO YOU NEED TO PAY?

For most freelancers the quarterly tax is applicable, but there are certain instances where you may be exempt from paying quarterly taxes.

#### 1

If you expect to owe less than \$1,000 in taxes after subtracting your federal income tax withholding from the total amount of tax you expect to owe.



#### 2

If your withholding amounts to 90% of the tax that you owe for 2010.



## HOW TO FILE YOUR TAXES

You are going to come across some interesting terms when filing your taxes as a freelancer.

### ASSET

An asset is something of monetary value that is used for your business. Some business assets you own can have their depreciated expense deducted.

### GROSS RECEIPTS

This is the total monetary income received as a freelancer before your expenses are subtracted.

### EIN

EIN is your employer identification number. Most freelancers will not have to worry about this number, but if you operate as a partnership or had any employees, you will need an EIN.

### PROFIT LOSS

### NET LOSS & NET PROFIT

If your business expenses are greater than your gross receipts for the year, then you have a net loss. If your gross receipts are greater than your expenses, you have a net profit.

### EXPENSES

Expenses are costs directly related to—and necessary for—the running of your business. If this is your first year as a freelancer you can deduct start-up costs.

### SCHEDULE C

Profits and losses from your freelance business are reported on your Schedule C form.

#### QUARTERLY TAXES

##### HOW TO FILE

WHEN	APRIL 15TH	JUNE 15TH	SEPT. 15TH	JAN. 15TH
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FORMS NEEDED	1040-ES
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WHERE	MAIL	EFTPS
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Electronic Federal Tax Payment System

##### ESTIMATING YOUR TAXES

A quick equation to estimate a quarterly tax payment:

$$\text{FROM YOUR MOST RECENT TAX RETURN: Total Tax} - \text{Withholding}$$

DIVIDED BY 4 (QUARTERLY)

May need to be adjusted if you feel your income may decrease or increase.

**TIPS** Try paying your estimated taxes monthly; you'll find the payments smaller and more manageable.

Once you're enrolled with EFTPS, you can electronically pay your quarterly taxes and never have to worry about a lost check.

Keeping a record of your estimated tax payment will make next year's estimated payments easier.

Do not forget to include your self-employment tax in your tax estimate.

#### ANNUAL TAXES

##### HOW TO FILE

WHEN	APRIL 15TH
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FORMS NEEDED	1040 SCHEDULE C	1040 SCHEDULE C-EZ	1040 SCHEDULE A
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WHERE	MAIL	EFTPS
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Electronic Federal Tax Payment System

**TIPS** It may be a good idea to seek the advice of a CPA who knows in the ins and outs of deductions for freelancers.

Remember: you can only declare a net loss 3 out of 5 years as a business before it is considered a hobby.

The number one most effective way to get through your taxes as a freelancer is to be organized. Keeping an accurate record will help you get the most out of your deductions and will protect you in case of an audit.

## FREELANCER AND DEDUCTIONS

Some of the greatest advantages to freelancing are the tax deductions you are allowed to take. Here are a few of the lesser known ones.

### UNPAID INVOICES

If you conducted business with a client who decided to disappear without paying the bill, you can write it off as bad debt. You will need to use the accrual method of accounting; further information is in IRS Publication 535.

### RESEARCH

Going to conferences, buying books, and other research-related expenses for your specific industry are all deductible.

### COFFEE MEETINGS

If you grabbed a cup of coffee with a client or a partner to discuss a project you can write off half of that expense. It may seem small, but those daily trips add up.

### JOB HUNTING

Any costs associated with job boards, joining a website to bid on a project, or any expenses associated with looking for new clients are deductible.

### PAYPAL FEES

If you had to pay any credit card transaction fees you can write off those fees as they are a necessary cost of doing business.

### HIRING ANOTHER FREELANCER

If you subcontract part of a project to another freelancer you can deduct the expense. Make sure to keep a record of the contract between you and the other freelancer.

### HOME EXPENSES

Payments towards utilities, insurance, mortgage interest, electricity and internet can all be deductible if you work out of your home.

### CELLPHONE

The first telephone line in your home can not be deducted, even if it is used for business. However, any secondary phones are a deductible expense.

### PROFESSIONAL ADVICE

If you sought advice from a professional, such as an accountant or lawyer, you can deduct his/her fees.

### SELF-EMPLOYMENT TAX

It may seem slightly counterintuitive, but you can deduct half of your self-employment tax on your income tax.

### HEALTHCARE

Medical expenses and health insurance premiums are deductible according to the requirements detailed in IRS Publication 502.

### CREDIT CARD INTEREST

If you purchased a big ticket item for your business on credit, the interest you pay for that equipment is deductible.