GETTING THROUGH TAX SEASON AS A FIRST-TIME FREELANCER

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Here's how not to let April 15 catch you by surprise.

By Brittany Taylor - March 16, 2015

Tax time is an easy enough concept when you're a full-time staffer: You fill out a W-4 when you start, you get a W-2 in January, and then you pick a tax software, answer its questions and start dreaming of what you're going to do with all the cash Uncle Sam's been slipping out of your paycheck. But when you go solo, life gets dicey. There's a whole new set of forms, a whole new set of taxes and a whole new set of rules. Yikes.

Before you give up on the IRS and pull the covers up over your head, hear us out. We interviewed a handful of fabulous accountants who specialize in filing taxes for creatives. Meet our tax guides: **Howard Samuels**, CPA MST, at Rosenfield and Co. in Florham Park, N.J.; **Jonathan Medows**, CPA, from New York City; **Andrew Poulos**, EA, ABA, ATP, from Atlanta, Ga; and **Gail Rosen**, CPA, PC, from Martinsville, N.J. Here, they answer frequently asked questions from inquiring, self-employed minds.

What is the 30 percent self-employment tax everyone talks about?
"When you work for a company, half of the social security tax comes out of your paycheck and the other half the employer has to match," Samuels says. "When you're self-employed, you have to pay it all. You are essentially the employer and the employee. All they did was change the terminology, calling it 'self-employment tax' instead of social security (or FICA) and Medicare."

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Self-employment tax comes out to roughly 15 percent. The rest of that 30 percent figure consists of federal and state income taxes, and while it's a good ballpark, it can vary depending on your location. For example, a freelancer in New England will likely pay a larger percentage of state income tax than a freelancer in Florida.

Where you work and/or live will decide how much and how many different taxes you need to pay. Medows, who himself is a Big Apple freelancer, says after the typical federal and state, he also is on the hook for city, regional and unincorporated business tax.

What about other items that would normally be taken out of my paycheck pre-tax, like health care and retirement savings?
Ah, benefits -- those are all up to you. "You can take [health insurance] as a deduction when you're self-employed," Medows says. That includes premiums for medical, dental and vision. "Same thing for IRA contributions, which have the potential to be tax deferred." Both decrease your tax liability.

Since we're talking about savings, also have plans in place for an emergency fund, just in case.

Will I be responsible for sales tax, too?
Here's where it can get tricky. Generally speaking, sales tax is charged only for tangible products -- something you can hold in your hand. If you're a graphic designer, for example, you typically would not have to charge sales tax for a digital file containing a business card design. However, if you were to print out 500 business cards featuring that design, then you *would* have to charge sales tax. Got it?

"Have plans in place for an emergency fund, just in case."

Say you *are* selling tangible goods to an end user. First, you'd go to your state and register your business. You'll receive a unique sales tax ID number. Depending on your sales volume, you'll remit the sales tax you've collected to the state on a weekly, a monthly, a quarterly or an annual basis.

"Every state has different laws when it comes to sales tax," Samuels emphasizes, so it's essential that you visit a CPA [aka a certified public accountant] to establish whether or not you'll need to start charging it. And if you do, he added, "It is very important that if you collect it -- even if you're late -- [that] you file it or you will go to jail. The state sees sales tax as their money -- so if you don't remit it, you're stealing from the state government."

Does this mean I need to hire an accountant?
"It depends," Medows says. "An accountant will help you take the right deductions, make sure you don't miss deductions or take things you shouldn't take. If you have any phobia about it, it's best to get professional help."

One other thing to keep in mind, Medow adds: "Sometimes it helps a freelancer to have a CPA relationship because later on, when they try to buy a house or borrow money, banks will insist on letters from their CPAs regarding their business. That can be difficult if you don't have a professional relationship."

If you *do* decide to go with a pro, Poulos urges you to find an accountant or tax professional who has experience and is licensed -- look for an Enrolled Agent (EA) or a CPA. Yep, those letters have real meaning. "Approximately 60 to 70 percent of the tax preparers around the country are unlicensed," he tells us. "A high amount of tax fraud and sometimes identity theft occurs from unlicensed tax preparers."

And look for one who's around for the entire year, not just during tax season, he advises. You'll want guidance if you happen to be audited or if you have questions about estimated taxes, sales tax or anything else that comes up throughout the year.

Expect to pay $200 to a couple thousand dollars, depending on the complexity of your tax return. Poulos tells us he charges a freelancer with 10 or fewer 1099s and fairly organized records between $325 and $375.

What makes the price go up? Samuels echoes the importance of organization. His firm supplies clients with a spreadsheet that has the various deductions and expenses set up in a template. You would fill this out before you go, ideally. Alternatively, you can bring your box of receipts and piles of invoices and let the accountant sort it out -- but this method will be far more expensive because, well, time is money.

What specifically do I need to keep track of?
Medows is emphatic about his No. 1: the money you earn. "Make sure you're collecting money from your clients. Sometimes freelancers just aren't on top of their receivables." In line with this is the amount you've paid throughout the year in estimated taxes.

Next on the list: "Expenses!" Medows says. "You have to save original receipts or scan images of them. That's a big deal for freelancers -- they get an audit, someone asks them to prove what they've put down and they don't have receipts. Credit card and bank statements are insufficient proof for IRS purposes."

"I advise all of my freelance clients to buy an accordion file and label each section with a different type of expense -- health care, marketing, office supplies and so on."

For an expense to be deductible it has to be "ordinary" and "necessary," Rosen says. Therefore, keep track of the money you spend on office supplies, business dues, business publications, accounting fees for your business, business cards, business entertainment (50 percent deductible), gifts (limited to $25 a person a year), postage, printing, continuing education computers, software, etc.

And don't forget about the business miles you drive. Log every trip -- starting point, ending point, the number of miles in between, and why you were driving there -- and decide how you want to deduct it. There are two methods, Rosen says: standard and actual. With the standard method, you can deduct a certain amount of money per mile ($0.56 in 2014), plus tolls and parking. The actual method is more complicated. First add up all of your automobile expenses and then multiple it by the percentage the car was used for business. To figure out the percentage, divide business miles by total miles driven for the entire year.

Needless to say, "organization can be a big problem," Samuels tells us. "I advise all of my freelance clients to buy an accordion file and label each section with a different type of expense -- health care, marketing, office supplies and so on. Make sure you get a receipt for *everything*... and put it in the folder. Then you're all set."

And how long should you hold onto all this paperwork? "Three years, per the IRS website," Medows says, "but if they ever accuse you of fraud, that can go back six years. I would err on the side of caution and say six years."

What happens if I mess up?
Nothing scary -- you're not going to go to jail (well, unless you hoard sales tax...).

"If you underpay, you might owe a penalty up to 10 percent," Medows explains. "If you overpay, they'll give you the money back (or you can put it toward next year's estimated taxes).

Concludes Medows: "The biggest problem I see when freelancers start out is they don't save money, and when it comes time to pay taxes, they don't have the money and they blow it off. The IRS will help you. They'll set up a payment plan. But if you don't have the money, don't not file. That'll just make a bad situation worse."

***Brittany Taylor** is a freelance writer. Find her on the Web at brittanymtaylor.com*