

# Tax Tips For Freelancers

**Small Business Tax Program**

**Brooklyn Coop FCU**

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**(718) 418-8232**

# Introduction



*la cooperativa de ahorro y crédito*

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**BROOKLYN  
COOPERATIVE**

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FEDERAL CREDIT UNION



# **WHO IS BROOKLYN COOP?**

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[www.brooklyn.coop](http://www.brooklyn.coop)

- **Federal Credit Union (FCU) serving Bushwick & Bed-Stuy since founding in 2001; expanded into the rest of Central Brooklyn and Ridgewood in 2017**
- **Community Development Financial Institution (CDFI)**
- **Mission: to build wealth, resilience, and opportunity by providing access to just and affordable financial services**
- **Committed to communities neglected by mainstream banking institutions**
- **Not-for-profit 501©1 with an affiliated 501©3 called Grow Brooklyn**
- **Member-owned (with over 8,000 members)**
- **NYC ID and ITIN are accepted in place of social security card**
- **We do not use Chexsystems**
- **The only non-profit providing tax preparation for small businesses and the self-employed**



# **BROOKLYN COOP'S SERVICES**

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- **Savings & Checking accounts for individuals and businesses**
- **Credit Cards**
- **Loan – personal, real estate, and small business**
- **Tax Preparation for self-employed individuals and small businesses**
- **Small business mentoring & workshops (free)**
- **Foreclosure prevention counseling (free)**
- **Individual credit review & financial counseling (free)**
- **Protect Your Treasure program (Power of Attorney, Wills, etc.)**

# **WHAT'S A FREELANCER?**



# WHAT'S A FREELANCER?

**A freelancer is an individual who, in the eyes of the IRS, is informally running their own business. They receive payments for their work without taxes withheld.**

**Freelancers are sometimes also called:**

- **Self-Employed**
- **Sole Proprietors**
- **Independent Contractors**

**Other more formalized business entities that are taxed the same way as freelancers are:**

- **Single-Member LLCs**
- **DBAs (Doing Business As)**
- **Disregarded Entities**

**Other business entities, (which that are taxed differently and have additional rules):**

- **Partnerships**
- **Multi-Member LLCs**
- **S Corporations**
- **C Corporations**
- **Not-for-profit Corporations**



**WHY ARE TAXES SO HIGH  
FOR FREELANCERS!?**

# WHY ARE TAXES SO HIGH FOR FREELANCERS!?

**All workers are required to pay about 15% of their income to the Social Security and Medicare funds. This is on top of regular income taxes.**

**EMPLOYEES** get to split this with their employer - the employee only pays 7.5% and the company pays the other 7.5%. This is a payroll tax called FICA.

**FREELANCERS** are both the worker and the company, so they're on the hook for the full 15%. This is called the self-employment tax and it's charged on your federal income tax return each year.

**EMPLOYEES** never actually receive the money they owe in taxes. Their taxes are withheld from their paychecks throughout the year.

**FREELANCERS** receive the full amount of their fee and pay their taxes all at once.

**So not only do freelancers owe more, it also “feels” like more because they actively pay it, no one is withholding the money on their behalf throughout the year.**

# **OTHER DIFFERENCES BETWEEN FREELANCERS & EMPLOYEES**

# **OTHER DIFFERENCES BETWEEN FREELANCERS & EMPLOYEES**

**Freelancers are not covered by unemployment, disability, or workers' comp. Employees are.**

**Freelancers have their income reported to them on Form 1099-NEC at the end of the year, employees receive W-2s which also report their withholdings.**

**Freelancers, like all businesses, can write off their business expenses to reduce their tax liability. Employees cannot.**

# **REPORTING BUSINESS INCOME**

# REPORTING BUSINESS INCOME

## The law:

- You must report all your business *income*, regardless of payment method or paper trail.
- How much you report in business *expenses* is up to you.
- In case of an audit, you must have records to prove your numbers.

**Cost of reporting income: higher tax liability**

## Benefits of reporting income:

- Social Security income later in life will be higher
- Clearly represent your business finances
- Presents a more formalized business
- Proves strength of business to lenders, investors, vendors, etc.
- You don't have to worry about getting in trouble with the IRS!

**Our Advice: Instead of underreporting income, track ALL associated business expenses throughout the year and be strategic about how many of them you write off.**



# **WHAT ARE BUSINESS EXPENSES?**



# WHAT ARE BUSINESS EXPENSES?

**You only pay taxes on *net profit* from your business:**

$$\text{Net Profit (or Loss)} = \text{Income} - \text{Expenses}$$

**Business expenses defined:**

- **Any amounts spent in connection with your trade, business, or profession**
- **This is straight out of tax law, (and it's quite vague!):**
  - **Must be “ordinary and necessary”**
    - **“ordinary” – common and accepted in your field of business**
    - **“necessary” – helpful and appropriate for your business**
  - **Must NOT be “lavish or extravagant under the circumstances”**

**The reason to claim business expenses is to lower your tax liability.**

# **HOME OFFICE DEDUCTION**

# HOME OFFICE DEDUCTION

- **Definition: space in your home which is used exclusively and on a regular basis for business – the space where you do your work and store your gear.**
- **A home office does not need to be separated by a wall or other partition.**
- **Expenses include the pro-rated portions of:  
rent, utilities, repairs & maintenance, homeowner's or renter's insurance, mortgage interest, real estate taxes, depreciation, etc.**
- **Expenses are pro-rated based on the size of your home office as compared to the size of your home, (i.e. if your office takes up a quarter of your home then 25% of your rent is deductible as a business expense).**
- **The home office deduction is taken last, after all other deductions have been calculated, and it can bring your profit down to zero but it cannot create a loss. Any remaining deduction can be carried over to the following year.**

# **BUSINESS MEALS**

# BUSINESS MEALS

- **Your food is only deductible at 50%, i.e. if you buy a \$10 sandwich at a lunch meeting, you can only write off \$5 of it.**
  - **Still track full costs, the pro-rating happens on the tax form.**
- **The cost of *all* meals while traveling overnight for business are deductible.**
- **When you're home, food is only deductible when eaten with another person, (co-workers or clients) for the purpose of recruiting or conducting business. Examples:**
  - **You can't just write off your lunch everyday because you ate it while working, another person needs to be involved.**
  - **If you chat someone up in line at the coffee shop and end up giving them your business card, though, that just became a business meeting, and your coffee is a business meal.**

The background is a soft-focus photograph of a city street at night. Warm, golden-yellow lights from buildings and street lamps create a bokeh effect. A person is visible in the distance, walking away from the camera. The overall mood is serene and urban.

# **TRANSPORTATION & LOCAL TRAVEL**



# TRANSPORTATION & LOCAL TRAVEL

- **Only job site to job site travel is deductible.**
- **The cost of commuting is NOT deductible. Commuting is defined as travel between home and your main job site.**
- **If you're traveling to different job sites all the time, then you have no *main* job site, and all your business travel is deductible.**
- **Pro tip: If you work from home (and take the home office deduction) then home is a job site, and that makes all business-related travel deductible.**
- **Expenses associated with alternate forms of transportation ARE deductible, to the extent they're used for business travel, (i.e. subway fare, taxis, CitiBike membership, bicycle maintenance, etc.)**





# **OUT-OF-TOWN TRAVEL FOR BUSINESS**

# OUT-OF-TOWN TRAVEL FOR BUSINESS

Overnight travel that is *primarily* for business and away from your “tax home” is deductible.

A deciding factor is whether you had control over the timing of the trip.

For example, did you go to Paris just to take photos you hope you’ll sell one day, (had control over the timing), or did you go to Paris to attend a conference which would happen with or without you, (did not have control over the timing)?

**Deductible expenses include:**

- Travel (flights, trains, buses, etc. to get there)
- Transit (taxis, subways, etc. to get around while you’re there)
- Lodging

If your trip is partially for business and partially personal, you can only deduct expenses for the days that were business-related.



# **PER DIEMS FOR OUT-OF-TOWN TRAVEL**

# PER DIEMS FOR OUT-OF-TOWN TRAVEL

**Instead of writing off actual expenses for lodging, meals, and/or incidental expenses, (M&IE), while traveling over night for work, the IRS allows businesses to write off daily per diems. Per diem amounts change based on location and month/year of travel. The maximum per diem amounts, set by the US Department of State, are published here:**

**Domestic per diems: <https://www.gsa.gov/travel-resources>**

**Foreign per diems: [https://aoprals.state.gov/web920/per\\_diem.asp](https://aoprals.state.gov/web920/per_diem.asp)**

**Incidental expenses are limited to fees and tips given to porters, baggage carriers, bellhops, and hotel staff.**

**In order to write off per diem amounts instead of actual expenses, you must document the time, place, and business purpose, but you do not need receipts.**

# **BUSINESS USE OF A VEHICLE**

# **BUSINESS USE OF A VEHICLE**

**You have the choice of writing off:**

- **a per mile deduction (changes annually, set by the IRS), OR**
- **actual vehicle expenses (pro-rated:  $\text{business miles} \div \text{total miles}$ )**

**Track all mileage and categorize it: business use, commuting, or other**

**^^ you need this tally no matter which deduction method you choose**

**Track all vehicle-related expenses: gas, oil, tolls, licenses, lease payments, insurance, garage rent, parking fees, registration fees, repairs, tires, etc.**

**If you want to depreciate the cost of your vehicle, then you'll also need to know: the original cost of the vehicle, sales tax paid, and date it was placed in service for your business**



# **OTHER BUSINESS EXPENSE CATEGORIES**





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# Other Business Expense Categories

**\*\* This is not an exhaustive list! \*\***

Use whatever categories make sense for you and your business.

- Advertising & Promotion
- Admission Fees
- Accounting & Bookkeeping Services
- Apps & Software
- Bank Fees
- Books, Magazines, & Publications
- Cell phone bill (pro-rated for business use)
- Commissions
- Computers
- Computer Accessories & Hardware
- Conference Fees
- Contract Labor (people who work for you)
- Costumes / Uniforms
- Credit Card Processing Fees (including PayPal, Stripe, etc.)
- Dues & Subscriptions
- Equipment Rental / repair
- Insurance (for your business, not health insurance)
- Interest Paid (on business debt)
- Internet (pro-rated for business use)
- Legal Fees
- Licenses & Permits
- Office Furniture
- Office Supplies
- Postage & Shipping
- Printing & Copying
- Professional Development
- Repairs & Maintenance (on your business gear)
- Rent & utilities on office space *outside* your home
- Supplies (specific to your industry)
- Tools
- Trade Show Booths
- Vehicle Rental

# **NON-DEDUCTIBLE EXPENSES**

# NON-DEDUCTIBLE EXPENSES

- **Fines, penalties, illegal bribes and kickbacks**
  - **example: parking tickets are NOT deductible!** 😞
- **Political contributions and lobbying expenses**
- **Personal expenses (but some are deductible as personal itemized deductions, discussed later)**

# **TAKING A LOSS**

# TAKING A LOSS

**If your business expenses are more than your business income, you can take a loss for the year on your taxes.**

**Taking a loss reduces your taxable income because you get to subtract that amount from any other income you have (i.e. W2 income, investment income, rental/AirBnB income, unemployment pay).**

## **Risks of taking a loss:**

**If you take a loss in 3 (or more) out of any 5 years, you are likely to be audited! The audit will not just ask for proof of your numbers (receipts, bank statements, etc.) but it will ask you to prove that you are “in business *with the intention* of making a profit”. This is subjective, will require essays, and is a big headache!**

**Remember, writing off expenses is not required. You can avoid this audit risk by writing off less expenses in some years to ensure that you show at least a small profit.**

**IN BUSINESS WITH THE  
INTENTION OF MAKING  
A PROFIT**



# IN BUSINESS WITH THE INTENTION OF MAKING A PROFIT

If you get audited and are asked to prove that you're in business with the intention of making a profit, these are some of the topics the IRS will consider:

- **Business manner.** Is the activity carried on in a businesslike manner? Are the books and records complete and accurate?
- **Time and effort.** How much time and effort is spent to make the activity profitable?
- **Dependence on the business.** Do you depend on the income from the activity for your livelihood?
- **The nature of the losses.** Losses are expected in the start-up phase. However, losses that appear to be within your control can raise some eyebrows.
- **Methods of operation.** Did you make any attempt to improve profitability?
- **The taxpayer's expertise.** Do you have the knowledge, experience, and education needed to carry on the activity as a successful business?
- **Track record.** Were you successful in making a profit in similar activities in the past?
- **Financial picture.** Does the activity make a profit in some years? How much?
- **Future profit.** Do you expect to make a future profit from the appreciation of assets used in the activity?



# **OTHER RELEVANT WRITE-OFFS (ADJUSTMENTS)**

# **OTHER RELEVANT WRITE-OFFS (ADJUSTMENTS)**

*These are not business expenses. They affect your AGI and your income tax liability only. They do not affect your self-employment tax liability:*

- **Monthly health insurance premiums**
- **Student loan interest**
- **Contributions to Traditional IRAs, SEP IRAs, and some Solo 401(k)'s**

**BUSINESS EXPENSES vs  
PERSONAL ITEMIZED  
DEDUCTIONS vs  
THE STANDARD DEDUCTION**

# **BUSINESS EXPENSES vs PERSONAL ITEMIZED DEDUCTIONS vs THE STANDARD DEDUCTION**

**Freelancers and businesses can deduct business expenses from business income and are only taxed on the profit. Net profit (or loss) from business is figured on Form 1040 Schedule C. The *self-employment tax* is calculated based on net profit from business.**

**After adding up all your income, including your net profit (or loss) from business, you subtract either the Standard Deduction or your Personal Itemized Deductions, whichever is higher. Your *income tax* is based on this remainder. (This is true whether you're a freelancer/business owner or not.)**

**Personal itemized deductions are figured on Form 1040 Schedule A.**

**Personal itemized deductions include:**

- **Medical costs**
- **Charitable contributions (to formalized 501©3 not-for-profit corporations)**
- **State & local income taxes**
- **Real estate taxes**
- **Mortgage interest**

**Each of the above are subject to various limits and are used only if they add up to more than the Standard Deductions.**

# 2022 FEDERAL STANDARD DEDUCTIONS

Filing Status	Amount
Single	\$12,950
Married Filing Jointly	\$25,900
Married Filing Separately	\$12,950
Head of Household	\$19,400

**Note that standard deduction amounts are set by the IRS, and they change each year.**

# ESTIMATED TAXES



# ESTIMATED TAXES

**Not everyone needs to pay quarterly/estimated taxes. There are two main reasons to do it:**

- 1. Avoid a large tax bill at the end of the year**
- 2. Avoid penalties for underpayment**

**If you want to avoid a large tax bill at the end of the year, pay any amount at any time.**

**If your intention is to avoid the underpayment penalty, you must pay by the deadlines. The deadlines for current-year estimated payments are:**

**April 15<sup>th</sup> (yes the same day last year's taxes are due!)**

**June 15<sup>th</sup>**

**September 15<sup>th</sup>**

**January 15<sup>th</sup> (of the following year)**

**Some basic (somewhat over-simplified) info about the underpayment penalties:**

- If your taxes owed at the end of the year are greater than \$1,000 on the federal side, or \$300 on the NY state side, you will be assessed a penalty.**
- The penalty is generally small. You can expect to pay about \$30 in penalties for every \$1,000 you owe in taxes.**
- To avoid the penalty, you must have paid either 100% of last year's taxes owed, or 90% of the current year taxes owed, throughout the year in the form of quarterly payments and/or withholdings.**
- The penalty is typically included in your final "taxes owed" amount, not billed separately, so you may be paying it and not even know.**

**PUTTING IT ALL  
TOGETHER**

# PUTTING IT ALL TOGETHER

Here's an outline of how your final "taxes owed" amount is calculated:

- **Business income – Business expenses = Profit (or loss) from business**

→ **Self-employment tax**

- **Profit (or loss) from business + Other Income – Adjustments = AGI (Adjusted Gross Income)**

- **AGI – Standard Deduction *or* Personal Itemized Deductions – QBI = Taxable Income**

→ **Income tax**

- **Income tax + Self-employment tax – Non-Refundable Credits = Tax Liability**

- **Tax Liability – Refundable Credits – Withholdings – Estimated Taxes Paid =**

**Taxes Owed or Refund Due**

# **RECORDKEEPING**

# RECORDKEEPING

**In order to file taxes as a freelancer, you need to keep your own records. At the end of the year, you'll need annual income totals *by client* and annual expense totals *by category*.**

**Throughout the year, you must keep a tally of:**

- **how much you were paid by each client**
- **how much you spent in each business expense category**

## **BENEFITS OF GOOD RECORDKEEPING:**

**Accurate Tax returns:**

- **Protected against an Audit or Tax Lien**
- **Able to identify maximum deductions**

**Able to pull financial reports quickly for grant and loan applications**

**Calculate the right sales price for your goods / services**

**Identifying Net Profit available to cover loans, staff, equipment purchase, etc.**

# **METHODS OF KEEPING GOOD RECORDS**



# **METHODS OF KEEPING GOOD RECORDS**

- **Receipts**
- **Notebook (vehicle logbook)**
- **Bank statements / credit card statements**
- **Excel**
- **Apps (for mileage tracking, invoicing, etc.)**
- **QuickBooks or other software**
- **Hiring a bookkeeper**



# Considerations

**Grow Brooklyn**  
[growbrooklyn.org/appointments](http://growbrooklyn.org/appointments)  
[freetaxes@growbrooklyn.org](mailto:freetaxes@growbrooklyn.org)  
718-418-8232 x6110

## **Volunteer Income Tax Assistance**

**VITA Hotline: 347-682-5606**

**Tues-Fri 11am-8pm**

**Sat 10am-4pm**

- \* **FREE income tax prep**
- \* **Must meet income eligibility**
- \* **Cannot claim:**
  - home office**
  - biz loss**
  - biz expenses over \$35K**

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- \* **Free initial consultations**
- \* **Affordable income tax prep**