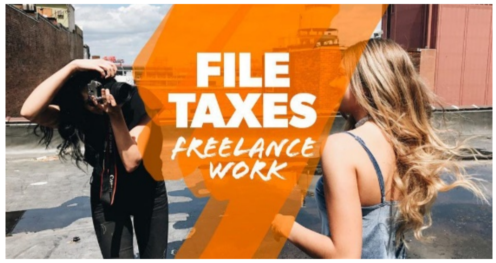
Freelance Taxes 101



Being a freelancer means being your own boss, and that can be awesome. You go out, kill something, and drag it home every day. That's how it's done, baby! And you're not alone. In fact, freelancers are expected to make up the majority of the U.S. workforce within the next decade.[1]

And why not? As a freelancer, you choose your hours, what projects to take on, and where you work. You get to call the shots!

But even if you already have a full-time job, freelancing is a great way to earn some extra money. And let's be honest, who doesn't want more cash in their pockets?

But here's some real talk: Whether you're a full-time freelancer or just getting your side hustle on, it *will* impact how you file your taxes. And if you're not careful, you could lose a large chunk of your freelance income to an enormous tax bill.

Tax Basics for Freelancers

What are the basics? There are three main things you need to know:

What's the minimum I have to earn to pay freelance taxes?

If you earn **$400 or more from freelance work** in any given year, you are responsible for paying taxes on those earnings**.** Dave recommends you save as you go by setting aside around **25–30% of every freelance check** you receive in a separate savings account to cover the taxes.

Why so much? Because you have to pay both income tax *and* the self-employment tax.

What is the self-employment tax?

The self-employment tax is **15.3%** and solely exists to cover your Social Security and Medicare taxes.[2]

At a normal full-time job, your Social Security and Medicare taxes are taken out of your paychecks automatically—and your employer covers half of those taxes. But as a freelancer, you're considered both an employee *and* an employer**.** That's why the IRS wants you to cover the whole 15.3%.

The Schedule SE tax form helps you calculate your self-employment tax, which you'll then report on your standard Form 1040. You might also be able to deduct the employer-equivalent portion (50%) of your self-employment tax on your 1040.

Remember, the self-employment tax is *in addition* to your regular income tax rate. That's why Dave recommends setting aside 25–30% out of your freelance checks in a separate savings account: because that'll cover both your income and self-employment taxes. This will keep you from getting hit with a huge bill at tax time.

When do I have to pay freelance taxes?

According to the IRS, you should pay taxes quarterly if you expect to owe at least $1,000 in taxes this year.[3] Since taxes from your freelance income aren't being withheld throughout the year, there's a good chance you'll need to estimate your taxes for the upcoming year and pay the IRS on a quarterly basis. The due dates for estimated taxes are:

Quarterly Tax Deadlines	
First Payment	April 15, 2020
Second Payment	June 17, 2020
Third Payment	September 16, 2020
Fourth Payment	January 15, 2021

So, how do you know if you need to do this or not?

That's a great question. Nearly half of all freelancers make $2,000 or less each year in freelance income.[4] If you fall within that group, you can probably skip estimated tax payments and just report your freelance income when you file your tax return.

But if it's looking like you'll owe $1,000 or more in taxes, Form 1040-ES can help you ballpark how much you'll make during the year and then determine your estimated taxes based on your projections.

If you underpay your estimated tax—these are *estimates*, after all—you'll have to pay the remaining taxes when you file your annual tax return. (And yes, freelancers must file an annual tax return by April 15—just like everyone else.) On the other hand, if you overpay your estimated tax, you'll receive the excess amount back in the form of a tax refund.

Keeping Track of Your Freelance Income

As a freelancer, you should receive a 1099-MISC from each client who paid you over $400.

However, many clients now pay freelancers and contractors through PayPal or other online payment systems, so you might receive a 1099-K form from your clients instead. But this form comes with an important caveat: Clients are not required to send you a 1099-K unless they pay you more than $20,000 or more than 200 times.

But just because you didn't receive a 1099 from a client doesn't mean you're off the hook. You still need to report your earnings to the IRS on a Schedule C form.

A Schedule C tax form serves as the hub for all your freelance income and expenses. First, you'll report *all* the freelance income you earned during the tax year in Part I. This includes amounts already reported on the 1099 forms you received from clients *and* amounts not yet reported from clients who didn't send a 1099.

After that, you'll list your expenses in Parts II–V to see if you can claim any deductions. If you had $5,000 or less in business expenses, the more simplified Schedule C-EZ might be best for you.

Self-Employment Tax Deductions

Tax deductions lower your taxable income, potentially reducing your tax bill and saving you hundreds of dollars in the process. And as a freelancer, you get to claim a bunch of them!

But many self-employed professionals aren't taking advantage of tax deductions. In fact, 73% of freelancers don't deduct any expenses at all.[5] That means some freelancers are paying more taxes than they have to!

As a freelancer, you can claim deductions on expenses that, according to the IRS, are "ordinary and necessary" for the operation of your business.

Some of the most common deductions for freelancers include:

- Advertising and marketing
- Office supplies
- Computer equipment and software
- Travel and business meals
- Home office
- Utilities

Careful documentation and detailed bookkeeping—like saving all your original receipts and invoices—can help you prove that those expenses were vital to your business, which will save you money come tax season.

That might be easier said than done since one in four freelancers has trouble keeping track of expenses.[6] One way to make the process simpler is to open a separate checking account specifically for freelance work. It's a great way to keep your personal and business finances separate—and track your expenses so you can claim them on your income taxes.

Sources:

https://www.daveramsey.com/blog/file-taxes-for-freelance-work