

Tax Strategies for the Newly Self-Employed

If you're a staffer turned contingent worker, you need to rethink your business status, retirement funding, and deductions

By Amy Feldman

It used to be that the vast majority of people worked in staff jobs. But in a tough economy, the number of independent contractors, temps, part-timers, and freelancers expands.

If you become a contingent worker, you'll need to rethink your taxes. For someone used to being on staff, "It's a mindset shift," says Eddie Gershman, a partner in Deloitte Tax's private client group. The common perception is that you'll pay more tax if you work for yourself, since you'll cover the employer portion of Social Security and Medicare taxes. While you will be on the hook for that self-employment tax, the tax advantages to working for yourself can soften the blow. Here's how to get the most out of deductions:

BEING A BUSINESS. As a self-employed person, you are now a business for tax purposes. That means you'll need to file Schedule C to calculate your business' profit (or loss) with your tax return. If you've got a profit on Schedule C, obviously, it's taxable; if you've got a loss, you may be able to use it to offset other income on this year's return—and, if you still have a loss, to offset income in previous or future years' tax returns. You'll also need to calculate your estimated taxes and file them quarterly.

FUNDING RETIREMENT. One of the easiest and most common ways to fund retirement when you work for yourself is with a SEP-IRA. Your contributions to the account reduce taxable income, similarly to when you had a corporate 401(k) plan. You can invest as much as 20% of net earnings from self-employment to the plan. Another, more complex option is to open an individual 401(k).

TAKING DEDUCTIONS. There are a lot of deductions and expenses that you qualify for as a business. Those self-employment taxes? Fifty percent are deductible. Your health insurance premiums? Deductible as well, under most circumstances. And, of course, you will get to write off business expenses for supplies, conferences, business lunches, and the like—so be diligent about compiling receipts. Capital expenses such as a new computer normally would have to be depreciated over time, but under a special small business tax break, Section 179, you can deduct up to \$250,000 worth of equipment.