Self-Employed

Generally, you are self employed if you:

- Operate as an independent contractor
- Are the sole proprietor of a business or you practice a trade
- In some way or another are in business for yourself

Things to know if you are self-employed:

- If you and your spouse operate a business together and file a joint return, both of you may be able to be treated as sole proprietors instead of as a partnership. Each spouse would report their share of income and expenses as a self-employed individual on the appropriate form (for example, Schedule C or Schedule F).
- Up to 100% of medical insurance costs you pay by for yourself, your spouse, and your dependents may be deductible as an adjustment to income on Form 1040, *U.S. Individual Income Tax Return*. The deduction is subtracted directly from your total income and applies whether or not you itemize.
- If you are self-employed and covered by a high-deductible health insurance plan, you may be able to establish a medical savings account (MSA). An MSA is a tax-exempt trust or custodial account that you set up with a U.S. financial institution (such as a bank or an insurance company) in which you can save money exclusively for future medical expenses. The distributions from MSAs are tax free if they are used for qualified medical expenses.
- If you use your vehicle for business purposes, you may be able to deduct expenses associated with such use. You may choose the actual expense method or use the standard mileage rate. If you choose the actual expense method, you must also keep track of your vehicle-related expenses for the year. Vehicle related expenses include gas, oil, insurance, repairs, cleaning, registration, etc. The business portion of your personal property taxes and vehicle loan interest is also deductible. Whichever method you choose, you must keep track of the mileage on your car from the first day of the year or the first day you use your car for business through the end of the year.

- You may be entitled to a tax break if you are operating a business from your home. The following questions will help you determine whether you can deduct the business use of your home:
    - Is this part of your home used regularly and exclusively in conjunction with your business or work?
    - Is this your primary place of business?
    - Is this where customers and clients meet with you?
    - Is this where you store product samples?
    - Is this where you administer or manage your trade or business?
    - If you answered yes to any of these questions, you may be able to deduct certain depreciation and operating expenses for the business use of your home. The same might apply if you use a separate structure, such as a shed.
    - You may recover your investment in certain business-related properties (such as equipment, a vehicle, or a building) through the use of depreciation. In this manner, you deduct some of your cost on each year's return. If you do not claim the depreciation, and later sell the property, the IRS calculates the basis as though you had taken the deduction each year. If you have unclaimed or have underclaimed depreciation deductions on property placed in service in prior years, you may be able to fully recover all allowable depreciation in the current year.
    - Up to $500,000 (for tax-year 2011) of certain tangible business property may be deducted in the year it was put in service (as a section 179 deduction) rather than using the depreciation method (section 179 expensing).
    - Your employees' wages and salaries are deductible if they are paid during the tax year for work directly related to your business and the pay is reasonable. You must be able to verify that the payments were made for duties actually performed. There are various types of withholding for different types of employees. Specific forms must be used for reporting payments made to employees.
    - You may be able to deduct expenses for a leased asset (such as a car or computer) used in your business. If it is not used solely for business purposes, you may deduct only the percentage of use that applies to your business or work.
    - Business tax credits can reduce your tax liability. There is a credit for providing access to the disabled and a work opportunity credit for providing work for members of groups with special employment needs or higher unemployment rates.

- If you are a freelancer writer, photographer, etc., you may qualify to use Schedule C, *Profit or Loss from Business*, as a self-employed individual and report your deductible business expenses on that form. If you took these deductions on Schedule A as an employee, they would be subject to a 2% of adjusted gross income limit.

- Costs that you have when setting up an active trade or business, investigating the possibility of creating or acquiring a business, and some legal fees are business start-up costs. You can choose to deduct up to $5,000 of business start-up costs with the remainder amortized over 15 years. Franchise fees, goodwill, and customer-based intangibles are also amortizable.

- If you use an accrual-basis method of accounting and you have been unable to collect money owed to your trade or business, you may be able to deduct that debt. You must have previously included the money owed as income so that you have a basis in the debt. A cash-basis taxpayer normally does not report income until they receive payment so they cannot deduct a bad debt.

- The tax implications of a self-employed individual are different from those of an ordinary wage earner. Each situation may present a number of complex tax questions.

- Certain individuals who are covered by a high deductible health insurance plan may be able to contribute to a health savings account (HSA). With this account, contributions are deducted from your gross income when calculating adjusted gross income, which means you do not need to itemize deductions to take advantage of this deduction. Additionally, distributions are not taxable if used for qualified medical expenses.