

TrainingPros

You Want to Be a Freelance Consultant?



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The purpose of this document is to provide prospective or current consultants an outline and a resource of the practices a professional might consider putting in place if they want to work as an independent consultant. Specifically, this document provides information and best practices for:

- Incorporating yourself
- Securing professional liability insurance
- Acquiring health insurance
- Setting up a home office

None of the information contained in this document should be considered legal advice or take the place of seeking legal counsel or other professional advisor/services.

INCORPORATION

As an independent contractor, you have the option of conducting your business with or without the protection of incorporating. Both circumstances have pros and cons associated with them. An unincorporated business owner is one in the same with their business. They personally bear all responsibility of the business. Incorporated businesses are usually sole proprietors or partnerships, are separate entities from the business owner, and have natural rights and responsibilities.

Benefits to incorporating:

- Limits your personal liability from company debts and obligations.
- Corporations have a reliable body of legal precedent to guide owners and managers.
- Allows you to potentially write off certain business-related expenses such as automobile, home office space, software and equipment, training fees, etc.
- Provides tax benefits under certain circumstances.

Considerations:

- Requires annual meetings and associated documentation.
- Entails expenses associated with incorporating.
- Requires periodic filings with the state as well as annual fees.

How to Incorporate:

1. Choose your business name and location: Choose an appropriate name for your new business and identify your headquarters' location. This doesn't necessarily need to be the state you live in or even where you expect to do the majority of your business, although choosing your home state may be an easier process. A CPA or incorporation attorney may be able to provide advice on which states may be most advantageous to you and your new business.
2. Decide how to structure your new business: Each structure has its own pros and cons; the best legal entity will depend on your business, location, and specific needs. Below you will find a short list of pros and cons for four of the most common business structures: Sole Proprietorship, Corporation, Subchapter S Corporation, and Limited Liability Company. If you are unsure of what structure is best for you, more information can be found on the [U.S. Small Business Administration](#) website and you should discuss with your CPA and attorney.
3. Form a board of directors: Once you decide the type of corporation, a board of directors may need to be established.
4. Obtain a Certificate of Incorporation: Certificates are available from your state's corporate filing office. This document will include your company name, purpose of the business, location, etc.

Corporate Filing Resources:

- Georgia: <https://georgia.gov/agencies/georgia-secretary-state>
- Texas: <http://www.sos.state.tx.us/corp/index.shtml>
- Illinois: <https://www.illinois.gov/Business/Pages/registration.aspx>
- Boston: <http://www.sec.state.ma.us/cor/>
- New York: <http://www.dos.ny.gov/corps/>
- New Jersey: <http://www.state.nj.us/treasury/revenue/filecerts.shtml>

5. File Articles of Incorporation: Along with the required registration fee, you will need to file the Articles of Incorporation your attorney has prepared with the office of the Secretary of State for your state.

Note: You have the option of filing all of the required paperwork yourself, through your attorney, or by using a third-party service (such as Legal Zoom). Choose the option with which you are most comfortable with and works within your budget.

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PROS AND CONS OF EACH TYPE OF LEGAL ENTITY

Sole Proprietorship – A sole proprietorship is the most common form of business organization. It is any unincorporated business owned entirely by one individual.

Pros:

- Easy to form
- Offers complete control to the owner
- Sole proprietors can operate any kind of business. It must be a business, not an investment or hobby but it can be full-time or part-time in nature.

Cons:

- Owner is personally liable for all financial obligations and debts of the business.
- Every sole proprietor is required to maintain business records to comply with federal tax requirements.
- Business income or loss is combined with other income and deductions and taxed at individual rates on your personal tax return.
- Sole proprietors must also pay self-employment tax on the reported net income.
- Sole proprietors do not have taxes withheld from their business income so you will generally need to make quarterly estimated tax payments if you expect to make a profit. These estimated payments include both income tax and self-employment taxes for Social Security and Medicare.

Corporation – A corporate structure is more complex than other business structures. The corporation is an entity that handles the responsibilities of the business.

Pros:

- Owner is generally not personally liable for the debts of the corporation.

Cons:

- More regulations and tax requirements
- More tax preparation services required than the sole proprietorship or the partnership
- Corporations are formed under the laws of each state and are subject to corporate income tax at the federal and generally at the state level.
- Any earnings distributed to shareholders in the form of dividends are taxed at individual tax rates on their personal tax returns.
- The corporation can be taxed and can be held legally liable for its actions.
- Income earned by a corporation is taxed at the corporate level using corporate tax rates.
- If a shareholder is an employee, they pay income tax on their wages, and the corporation and the employee each pay one half of the social security and Medicare taxes and the corporation can deduct its half.

Subchapter S Corporation – The Subchapter S Corporation is a variation of the standard corporation. The S corporation allows profit or losses to be passed through to individual tax returns similar to a partnership. An S corporation has the same corporate structure as a standard corporation. It is a legal entity, chartered under state law, and is separate from its shareholders and officers.

Pros:

- Limited liability for corporate shareholders
- Generally, exempt from federal income tax other than tax on certain capital gains
- Generally, taxes are not paid at the corporate level.

Cons:

- The income flows through the shareholders' individual returns.
- Taxes are due on your share of corporate income, regardless of whether it is actually distributed.

Limited Liability Company (LLC) – A Limited Liability Company (LLC) is a relatively new business structure allowed by state statute. LLCs are popular because of the great combination of flexibility and protection associated with them. They shield members from personal liability while affording them an array of tax options.

Pros:

- Owners of an LLC are called members. Since most states do not restrict ownership, members may include individuals, corporations, other LLCs, and foreign entities. Most states also permit "single member" LLCs, those having only one owner.
- Tax Flexibility: The IRS does not consider an LLC to be a distinct separate entity for tax purposes. Members of the LLC get to determine how they want to be taxed.
- Generally, members of an LLC will create an operating agreement that outlines how the LLC will be treated for tax purposes. Further information on how the IRS classifies some LLCs can be found at [IRS.gov](https://www.irs.gov).
- Less Paperwork: Compared with other business entities, LLCs are very flexible.
- With less stringent compliance requirements and less required paperwork, LLCs are easier to form and easier to keep in good legal standing.
- Limited Liability: Like corporations, LLCs provide their members protection from liability. This means that members are not personally liable for debts and/or court judgments incurred by the LLC.

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Cons:

- Self-Employment Taxes: Unless you choose to be taxed like a corporation, LLCs are usually subject to self-employment taxes. This means that the profits of the LLC will not be taxed at the corporate level, but will pass through to its members who will account for those profits on their personal federal tax returns.
- Often times, these taxes are higher than they would be at the corporate level.
- Individual members will pay for federal withholding such as Medicare and Social Security.

PROFESSIONAL LIABILITY INSURANCE

Professional liability insurance is a form of insurance that helps protect professional advice and service providing individuals and companies from bearing the full cost of defending against a negligence claim made by a client. The coverage focuses on alleged failure to perform on the part of or financial loss caused by the policyholder. These are causes for legal action that would not be covered by a more general liability insurance policy, which addresses more direct forms of harm.

Professional liability coverage sometimes also provides for defense costs, including when legal action turns out to be groundless. Professional liability insurance is required by law in some areas for certain kinds of professional practice and is also sometimes required under contract by some businesses.

How much coverage should you carry? The recommended amount is somewhere in the range of \$250,000 to \$500,000. A conversation with your insurance broker will help you determine the exact amount to protect you or your corporation.

NOTE: Hiring an insurance broker comes at no cost to you, the policyholder. An insurance broker can advise you on the types of insurance and amounts of coverage you should carry. Further, an insurance broker will research and propose insurance companies to provide the policies you may need for your business. Finally, the insurance company pays the insurance broker, i.e., there is *no cost to you to hire an insurance broker*. Let them do the legwork!

CPA

While doing your own taxes will certainly save you money, once you decide to own a business, the benefits of using a CPA (Certified Public Accountant) may outweigh the costs involved.

The first, and most important, benefit to using a CPA is the value added by their vast knowledge and understanding of the tax code. The expert advice that you receive from your CPA will likely translate into potential savings on your taxes. In this regard, hiring a CPA can be viewed as an “investment.”

In addition to the cost savings, a CPA is far more experienced at handling complex tax issues and can complete the work in a fraction of the time that it would take you to file them on your own.

The fees associated with using a CPA will vary based on the complexity of your individual tax preparation. However, you can expect to pay somewhere in the range of \$200 – \$400 per quarter for a CPA to prepare and file your business tax returns.

HEALTH INSURANCE

If you do not have a spouse/partner through whom you can get health care coverage, we recommend finding a broker who can be your advocate for selecting a plan that best fits your needs. The health insurance company, not you, pays a broker for their services. In Georgia, where TrainingPros is based, we recommend the Health Plan Store – [www. Healthplanstore.com](http://www.Healthplanstore.com).

OFFICE SETUP

The following are recommendations for setting yourself up with a home office:

- Office Space: Create an office or work space that provides you a quiet place to work free from distractions.
- Separate landline: you can add a line to your existing service for a minimal monthly cost or, at a minimum, ensure your home voicemail announces you and your business name to potential clients when they call.
- Fax line: If your clients will require you to send faxes, consider buying a scanner and subscribing to an e-fax service.
- Computers: Windows based computers are suitable for most jobs. However, consultants in creative roles, such as graphic designers, should consider working with a MAC.
- Software: You will need the most up-to-date version of any software your client is expecting you to use.
- Marketing and Self-Promotion: Two key factors in establishing yourself as a freelance consultant are marketing your work and making yourself visible to potential clients. We recommended you accomplish these goals through a professional website or high quality portfolio (hard copy and digital) and a strong presence on popular recruiting sights such LinkedIn and Glassdoor.