

THE FREELANCER AND BUSINESS GROWTH: BEST PRACTICES

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independence and autonomy redefined

Introduction

It is common knowledge that the primary cause for business failure during the first year as a Solopreneur is inadequate back office support. Although fear for lack of income stability is the most important reason for hesitance in making the Big Step to independence, most Freelancers know how to generate income once they are in business for themselves. Estimates of what percentage fails as a result of insufficient support and lack of controls range from 25 – 50%. Whatever the exact number is, it is unnecessarily high.

Not knowing the unknown

When contemplating a future as a Solopreneur, often people don't know where to start in terms of building a support infrastructure, nor what to include. There also seems to be an almost automatic propensity toward self-help, combined with a tendency to postpone action steps when it comes to setting up an

operational infrastructure and financial controls. As a consequence, the business is likely to get into uncharted waters soon after start-up, which may result in unpleasant surprises, such as tax claims and unexpected financial and/or legal obligations. Ironically, the more successful the freelancer is, the sooner

problems are likely to surface. Early stage confrontations with such hick-ups can lead to an abortion of the start-up that could have been avoided. Of course, later stage growth will also stress test the back bone of the mini enterprise. Ergo, it is never too early to ensure that your business has an appropriate foundation and has it's 'back of the house' in order.

Key building blocks

1 - IT Infrastructure

An IT infrastructure is a fundamental portion of any business foundation. Getting the right equipment and software – however simple it may be, deserves careful planning and forethought. Consider what the contemplated 'Front of the House' and 'Back of the House' functions are. The 'Front of the House' is obviously externally oriented toward acquiring and maintaining client relationships and includes sales, marketing, CRM, website, etc. The 'Back of the House' has support functions ranging from

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basic office tools to billing, collections, bookkeeping, order tracking / time sheet / SOW tracking. A rule of thumb is not to use anything but dedicated hardware and software. In other words, don't use your home computer. Another rule is making sure that you install data back-up devices and disciplines. Lining up professional support right from the start is important, too, so that you don't have to scramble when – not if – IT problems arise. Of course, completely hosted environments – 'cloud' computing – are available and represent an ideal solution for the Solopreneur. Using Software as a Service (SaaS) and secure, remote storage facilities is convenient (your 'office in the cloud' is always available, from anywhere; all you need is access to a browser) and can prevent quite a few of headaches, because you do not have to operate or maintain any hardware or software other than the device you use to access the Internet.

2 - Self Incorporation

Should you incorporate? LLC or S-Corp? These are frequently asked questions among Solopreneurs and Freelancers.

The answer to the first question is yes. It would be best to establish a legal entity. Reasons are liability protection, tax advantages, business status/legitimacy and keeping your private and business finances separate.

The primary reasons to elect an S-Corp would be related to multiple shareholders and high income. If you are a Freelancer with anticipated billings of less than \$250k per year, an LLC is your legal entity of choice. An LLC is simple to establish and provides the same liability protection as an S-Corp. Further, the LLC can qualify as a 'disregarded' entity for income tax purposes, assuming it is appropriately configured. In that case, the net of revenues and business expenses flow directly to the LLC's owner and should be reported in his or her personal tax return; in other words, no corporate tax returns are filed. Of course, as the owner / operator of an LLC, the Freelancer will have to pay self employment taxes.

Setting up a professionally configured LLC and ensuring proper tax treatment does require expert guidance. In today's 'self help' environment, many ads suggest that you 'simply go on line' and 'click' your way to a low cost solution. For something as important as establishing a business, professional legal, tax and accounting guidance is a must.

3 – Financial controls

As a freelancer, very important is - besides establishing the right IT infrastructure - to have a simple set of accounting books. You can't fly the plane without a dashboard. Quick insight into your payables, receivables and cash balance plus a basic invoicing system are prerequisites for the health of your business. Also here, simple accounting software is available for 'do it yourself' purposes, but you may want to briefly involve an accounting expert to make sure that your chart of accounts has been set up right from day one. After that, absolute discipline in keeping the financial records up to date should never fade.

4 – Health Plan

Navigating the world of health insurance can be challenging. Not only is this a topic that has been in the socio-political lime-light for a long time, it is also a subject that is a source of confusion and misunderstandings.

The first misconception is that 'group' plans reduce cost. Although economies of scale may save some administrative costs, joining a group doesn't make someone healthier or sicker. The group merely averages demographics. In other words, if you are young and healthy you overpay as a group member, whereas older, less healthy members benefit from group membership. Groups may offer advantages for people with 'pre-existing' conditions, while on the other hand, the group plan determines what benefits the members get, leaving little personal choice and options.

Fortunately, the market for individually underwritten plans has become a lot more robust over the last several years; more plans are offered by more carriers. There has been a trend toward 'consumer driven' product design. 'High deductible' arrangements and HSA's are examples of an orientation toward the individual in product design.

The Freelancer in search of health coverage can expect to be confronted by simple market realities; if you are a 26 year old marathon runner, your premiums will be lower than if you are 60 years old and overweight. That is not the fault of the system, but the result of a difference in cost of health care between the two examples.

The best way to navigate the market is:

- A) By working with best of class brokers. Compare what independent brokers offer to quotes from agents who represent a carrier;
- b) By combining products. For example, a combination of a Defined Benefit Plan and a High Deductible, 'catastrophic coverage' layer of insurance may offer what you need.

5 - Retirement Plan

As a business owner, it can be possible to make pre-tax retirement contributions as an employer AND employee. Also here is an example where expert advice should be used to ensure that the plan design is in compliance with the tax code.

Growing your business

When success as a Freelancer reaches a point where growth triggers the need for help, it can be advantageous to contract another self-incorporated Freelancer and establish a b2b relationship between the two LLC's, rather than hiring the person as an employee.

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