

How To Effectively Manage Your Freelance Income



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One of the toughest things about freelancing is figuring out how to manage your freelance income so that you're not standing in line at the local food bank during the lean times (although that's an option, and it's certainly happened!). Here's a how-to guide to help you smooth out the roller-coaster ride of your cash flow.

Open a Separate Business Account With Multiple Savings Accounts

Let's talk about bank accounts for a minute. In addition to your personal checking account, it's a good idea to set up a separate business account. This makes it easier for you — and your accountant, if you have one — to manage your freelance income. This will make your accountant very happy, come tax season.

In addition to your main business account, most banks will allow you to set up multiple savings accounts for free, so why not take advantage of this ability? Even though you can manage your freelance income using bookkeeping software or spreadsheets, squirreling your savings away in separate accounts isn't a bad idea, if for no other reason that it might make you think twice before getting your hands on money that you're setting aside for stuff other than splurges. Especially if, like me, you put the checkbooks and debit cards in one of those "perfect" places that you can never find afterwards.

Here's a suggested list of bank accounts to consider opening:

- **Main Business Account:** Make this the highest-yield savings account your bank offers, so that any cash that's in there is earning interest while it's sitting there. When a client pays you, this is where you deposit the check. From this account, you:
 - Pay yourself
 - Pay your business expenses
 - Set aside money for taxes, retirement and emergencies

- **Savings Accounts to Open Under Your Business Account:** Open the following savings accounts under your main business account, and then once a month, after you pay yourself, transfer a designated amount into each of them. Think of these transfers simply as additional bills to be paid. I believe that most banks will even allow you to automate these transfers, which makes it a pretty painless and darn convenient way to manage your freelance income.
 - **Retirement Savings:** This can be a traditional retirement account such as a 401K, or you could even start doing a little basic investing with this money, since (hopefully) it's going to be in there for awhile.
 - **Tax Savings:** This is the holding area for yearly taxes
 - **Emergency Savings:** This is your buffer for lean times.

Set Up an Emergency Fund

Your emergency fund should be the first thing you think of when you have any cash left over after your expenses are paid. Having a year's worth of expenses in reserve is a worthwhile goal for effectively managing your freelance income. Your emergency fund will be there for you in case your income drops below what you need to keep your commitments. In addition, having an emergency fund means that you can turn away clients who don't quite feel right, or if a good client runs into a financial tight spot and can't pay you immediately, you'll have a cushion to carry you through. And of course, there are those unforeseen things that just happen — called emergencies — such as a pet getting sick or an unexpected car repair.

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Treat yourself like an employee

Decide how much you can afford to pay yourself, then on a regular basis, either write a check to yourself or set up an automatic transfer from your business account and deposit it in your personal checking account. It is from your personal checking account that you pay things like rent, food, and other living expenses that aren't related to the business.

When deciding how much to pay yourself, it's a good idea to stay on the frugal side and only pay yourself enough to cover your living expenses plus a little extra, then sock anything that's left over at the end of the month into your emergency fund.

Project Upcoming Monthly Income and Expenses

Part of effectively managing your freelance income is figuring out how much money you're making and spending each month, and then using those numbers to estimate what the next year might look like. When you're calculating your projections, it's a good idea to base your budget on your **lowest monthly business income** and **highest monthly business expenses** from the previous year. This is like assuming the worst-possible scenario, and hopefully, if your income's trend is generally upward, estimating conservatively in this way should give you a bit of a buffer, which, once again, you can sock away in your emergency fund. It's impossible to have too much money in that emergency fund!

Break Up Client Payments for Big Projects

If you're working on a big project that extends over multiple months, consider billing your client on a time-interval or a "milestone" basis. That way, if your client flakes out or can't pay you immediately, you're only out a partial payment instead of the whole thing at once. It also smooths out your income curve, making budgeting easier. Also, if you need to exert a little persuasive power on a particularly recalcitrant client, you can calmly explain that they'll get no more work from you until you're paid from the last billing cycle. Hopefully you'll never need to use this tactic, but it's there if you need it.

Be creative in finding ways to generate additional income.

There's a whole movement called the [Share Economy](#) that you can tap into for additional sources of cash at little or no cost to you. If you have an extra room in your house, consider [renting it out to travelers](#), or [rent your car](#) when you're not using it. Or consider investing some of your leftover money in things that appreciate in value, such as musical instruments, that you can sell later for a profit. The more different streams of income you have, the less of a hit you'll take during a dry spell in freelancing.

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If possible, live on only one income.

If you have a partner with a job or other regular stream of income, do your best to live on that income alone, and either save or invest everything that you earn from freelancing.

Establish a foundation of thrift.

You never know when you're going to have a lean month, or even a lean year, so make a habit of living on the cheap. Sign up for Netflix instead of paying for cable TV. Buy clothes at a thrift store, or check out local garage sales for things like furniture, sports equipment and appliances. Avoid buying fancy tires and rims for your truck that are going to cost a fortune to replace later. Trade stuff that you don't want for stuff that you do want on [Listia](#).

Resist "lifestyle inflation".

This is the temptation to increase your spending as your income increases. If you find yourself at the end of the month with money left over, stash it in your emergency fund or invest it back in your business by, say, paying for some online advertising or attending a seminar in your field of expertise.

Prioritize spending.

Many financial experts recommend sitting down and writing down your expenses. Prioritize them according to importance and pay the most important ones first.

Pay down your debts.

Take a piece of paper and divide it into columns. List your largest monthly payment toward the left, then go smaller and smaller until your smallest monthly payment is at the far right. Double up on the smallest payments until that debt is gone. Then take the money that you're no longer spending on that debt and start doubling up on payments on the next debt. Keep going until all of your debts are paid off.

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