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IN FOCUS

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Tax Treatment of Gig Economy Workers

The gig economy (or sharing economy) is a form of work relationship that has become popular in recent years. Gig economy workers earn income by providing on-demand work, with "gigs" often facilitated through digital platforms. This In Focus provides an overview of how gig economy workers are taxed and reviews recent legislative changes.

What Is the Gig Economy?

There are three parties to a gig economy transaction: the worker, a digital platform, and a consumer. Digital platforms, such as Uber, Airbnb, DoorDash, and TaskRabbit, match workers with consumers and often process payments. Many platforms also set rates for work. Because the digital platforms act as intermediaries, workers and consumers often have less interaction with each other (in terms of advertising, contracting, payment processing, etc.) than in other freelance business relationships.

Participation in the gig economy is widespread. Although the major digital platforms are the best known, many gigs predate the internet and do not use digital platforms. For more on the gig economy and what it means for workers, see CRS Report R44365, *What Does the Gig Economy Mean for Workers?*

The tax treatment of gig economy workers is very similar to that of other self-employed workers. The gig economy is sometimes called the "1099 economy," named after the series of IRS forms that income is reported on. The particular Form 1099 that gig economy workers receive depends on the work they do and the platform's legal structure. In many cases, a gig economy worker (and the IRS) will receive a 1099-NEC (a new form that replaced some functions of the 1099-MISC) or 1099-K from a platform they perform services for. Gig economy workers are independent contractors—broadly, workers who provide a service but are not employees of the organization. (In contrast, traditional employees are sometimes referred to as "W-2 employees" reflecting the information return on which their employee compensation is reported.)

What Taxes Are Gig Economy Workers Subject To?

Gig economy workers are generally subject to the same taxes as other self-employed individuals. They calculate their liabilities and pay any unpaid taxes as part of their individual income tax returns (i.e., IRS Form 1040). Gig economy workers owe federal income tax and social insurance taxes on income they receive, comparable to the taxes W-2 employees owe. (For self-employed workers, social insurance taxes are often referred to as "self-employment" taxes, discussed below.) Since gig economy workers are often paid as independent contractors, the tax code treats gig economy workers like sole proprietors, the single employee of an unincorporated small business.

Income Taxes

Gig economy workers have the same federal income tax obligations as traditional employees, and are subject to the same tax rates. Net income from gig economy work (revenues less deductions) is subject to federal income tax, even if the platform does not report it to the IRS.

Income tax deductions. Gig economy workers are eligible for the same deductions available to other small business owners. This allows gig economy workers to deduct certain operating costs to determine net business income. Some deductible expenses include business-related mileage in a personal vehicle, equipment and materials needed for work, and the use of a home office. Gig economy workers may also deduct half of self-employment taxes paid as an above-the-line deduction on their individual income tax returns. These deductions are available to gig economy workers whether they itemize their deductions or not.

Many of these deductions are not currently available to traditional employees. The 2017 tax revision (commonly referred to as the "Tax Cuts and Jobs Act" or TCJA; P.L. 115-97) temporarily repealed the deductibility of unreimbursed expenses incurred by an employee for tax years 2018 to 2025 (through the limit on miscellaneous itemized deductions).

Qualified Business Income deduction. The TCJA created the Qualified Business Income (QBI) deduction. The QBI deduction allows many gig economy workers to deduct 20% of their net business income from their taxable income. The QBI deduction is available to pass-through businesses with certain income and structure requirements. The deduction is available to taxfilers regardless of whether they itemize deductions and is generally calculated based on net business income (i.e., income less all deductions, including half of self-employment taxes).

Self-Employment Taxes

Gig economy workers owe self-employment taxes, a term that generally refers to Social Security and Medicare taxes paid by self-employed workers. Traditional employees pay comparable taxes, statutorily splitting them equally with their employers. Gig economy workers, like self-employed workers more generally, must pay the employee and employer portions themselves. For most gig economy workers, the tax rate is 15.3% (12.4% for Social Security and 2.9% for Medicare) on net earnings from gig economy work. However, as previously discussed, gig economy workers may also deduct half of these taxes as an above-the-line deduction on their federal tax returns.

Gig economy workers owe self-employment taxes if they have net earnings (earnings minus deductions) of $400 or more from self-employment, even if the income is not reported to the IRS. The Social Security portion of self-employment taxes is combined with wage income toward the annual income maximum for the Social Security tax ($142,800 in 2021). There is no income maximum for the Medicare portion.

What Are the Platforms' Reporting Requirements?

Many of the major digital platforms have taken the position that they qualify as "third party settlement organizations" (26 U.S.C. §6050W). Under prior law, a *de minimis* threshold provided that such organizations only needed to report the income a gig economy worker received to the IRS if the worker earned more than $20,000 on the platform *and* conducted more than 200 transactions within a calendar year.

Relatively few gig economy workers—especially those whose gig economy work supplemented their income—met these thresholds, so their income from platforms was not reported to the IRS. Tax noncompliance is higher when income is not subject to third-party reporting. A GAO report (GAO-20-366) published in 2020 recommended that the IRS evaluate reporting thresholds to improve tax law compliance for gig economy workers.

The American Rescue Plan Act of 2021 (P.L. 117-2) significantly lowered this *de minimis* threshold. Starting in 2022, platforms will be required to report to the IRS payments to workers that exceed $600 in a calendar year. The new reporting threshold for third party settlement organizations is the same as the threshold for payments made by other businesses (26 U.S.C. §6041). The Joint Committee on Taxation (JCT) estimated this policy change would increase federal tax revenue by $8.4 billion from FY2021 through FY2031.

How Can Gig Economy Workers Meet Their Tax Obligations?

In general, taxpayers pay their income tax liability as income accrues over the tax year, and in advance of filing their tax returns. This is typically done through automatic withholding from employees' paychecks, or quarterly estimated tax payments on other taxable income. Gig economy workers who expect to owe taxes on their gig economy income make quarterly estimated tax payments to the IRS. Failing to do so can result in the taxpayer having to pay these taxes when filing their individual income tax return *and* owing an underpayment penalty. Calculating the amount of the underpayment penalty can be complex and is usually done by the IRS.

Gig economy workers have several options to pay taxes owed on their gig economy work. Such workers who also have a traditional job can file a new Form W-4 with their employer, requesting a larger automatic withholding to cover the taxes on their income from gig economy work.

Gig economy workers who are not also traditional employees generally need to file quarterly estimated tax payments. Generally in April, June, and September of the tax year and the January of the following year, a quarter of the worker's annual estimated tax bill is due to the IRS. This amount includes income tax and self-employment tax liabilities.

Are Gig Economy Workers Eligible for the EITC and Other Tax Credits?

Gig economy workers' eligibility to participate in government programs varies by program. Generally, gig economy income is treated as self-employment income for many programs.

Gig economy income is considered "earned income" for calculating eligibility for, and the amount of, the Earned Income Tax Credit (EITC). Hence, gig economy net income may result in a larger or smaller credit, depending on the taxpayer's adjusted gross income, number of qualifying children, and filing status. Gig economy income used to calculate the EITC must be included on a tax return, even if it is not reported to the IRS by a platform. Gig economy income may also affect eligibility for, and the amount of, the child tax credit and the child and dependent care credit.

What Tax-Advantaged Options Do Gig Economy Workers Have for Health Insurance and Retirement Savings?

Gig economy workers who meet the requisite eligibility requirements may be eligible for Medicaid or premium tax credits to purchase health insurance through the health insurance marketplace. Gig economy workers who pay out of pocket for all or a part of health insurance premiums may qualify for a self-employed health insurance deduction. This above-the-line deduction can be used whether or not the worker itemizes deductions.

Gig economy workers may qualify for a variety of tax-advantaged retirement savings options. Individual Retirement Arrangements (IRAs) are available to everyone who meets eligibility requirements, not just self-employed workers. Other plans, such as a SEP-IRA, one-participant 401(k), or SIMPLE IRA, offer other opportunities for gig economy workers to save for retirement in tax-advantaged accounts. Gig economy workers with relatively low incomes from all sources and who meet other requirements may be eligible for the Retirement Savings Contribution Credit.

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