ADVISORY SUMMARY · FOR DISCUSSION WITH YOUR CPA OR EA

The S Corporation Election

What changes when your LLC elects S corporation tax status, what it can save, and what it asks of you in return.

Prepared for you by ______________________ Date __________

Your LLC stays an LLC. Nothing changes with the state, your contracts, or your liability protection. The election changes how the IRS taxes the business: you become a W-2 employee of your own company, paid a reasonable salary, and you take the remaining profit as a distribution. The points below are a starting framework for a conversation with your CPA or EA, not final tax advice.

1. The core advantage: the salary and distribution split

In a default LLC, all net profit is subject to self-employment tax of 15.3 percent for Social Security and Medicare. After the election, only the salary carries that tax; the distribution above it does not. The more profit the business earns above a reasonable salary, the more the split saves.

ITEM	DEFAULT LLC	LLC TAXED AS S CORP
Net business profit	$120,000	$120,000
Reasonable W-2 salary	Not applicable	$70,000
Profit taken as distribution	$0	$50,000
Income exposed to the 15.3% tax	$120,000	$70,000
Approximate self-employment / payroll tax	~$16,955	~$10,710
Illustrative annual savings		**~$6,245**

Hypothetical, rounded figures for tax year 2026, before the added costs of running payroll. Your result depends on your salary, your state, and your filing situation.

2. The salary is the lever, and it has to be defensible

The salary is not a number you pick to maximize savings. The IRS requires reasonable compensation for the work you actually do, and documented figures often land around 40 to 60 percent of profit. That is why this example pays $70,000 on $120,000. Your CPA or EA can run this same math on your numbers and your state with the calculator behind this summary; the salary that comes out of that conversation is the one worth documenting.

3. What else the election brings

Accountable plan reimbursements.
As a W-2 employee, the company can reimburse you tax free for business use of your home office, vehicle, phone, and internet under a formal accountable plan.

Deductible employer payroll tax.
The employer half of Social Security and Medicare on your salary is a deductible business expense.

Pass-through treatment is preserved.
An S corporation is not taxed at the entity level in most states, so you avoid C corporation double taxation.

The QBI deduction is retained.
The 20 percent qualified business income deduction remains available to S corporation owners, subject to current Section 199A rules and income thresholds.

Retirement flexibility.
A W-2 salary can support employer retirement contributions, such as the employer portion of a Solo 401(k).

W-2 formality.
A regular paycheck with withholding can simplify personal cash flow, estimated taxes, and mortgage qualification.

4. The other side, stated plainly

Payroll and compliance cost money.
Running payroll and filing an 1120-S return adds annual cost, and the savings have to clear it.

Reasonable compensation is required, not optional.
The salary is the number an examiner looks at, and it needs documentation behind it.

A low salary can backfire.
Where Section 199A wage limits apply, cutting salary too far can shrink the QBI deduction and cost more than it saves.

It does not pay everywhere.
Some states and some fact patterns, including lower profit levels, make the election a wash or a loss. The calculator models both directions.

> **Next step.** Ask your firm to run the calculator on your numbers and your state, and to walk through both totals with you. If the election makes sense, the next piece of work is documenting the salary: a written reasonable compensation figure with the methods and working papers behind it, prepared through your firm and delivered under its name.