

Payments made to business owners from their business depend on the type of business entity, so this paper is to explain payments applicable to S Corporation Owners (called Shareholders).

There are five basic types of payments that may be made to S Corp owners from their business and the tax implications are different so want to be clear on which is which to avoid tax issues.

- 1) **Payroll** – S Corp owners are paid payroll same as all employees and pay all of the same payroll taxes including FICA (Social Security & Medicare), FUTA (Federal Unemployment) and SUI (State Unemployment) although some states do not require this last one, so do check with your state to find out if there is any exemption for S Corp business owners.
 - a. Social Security is 12.40% of Gross Pay up to an annual limit (see IRS website)
 - b. Medicare is 2.90% of Gross Pay and an additional .9% for Gross over \$200k
 - c. These two are paid half by employee and half by employer (6.2% & 1.45%)
 - d. FUTA is \$42 a year and SUI varies by state (\$245 in CA), all paid by employer
 - e. Payroll is also subject to Federal and State Income taxes paid by employees

- 2) **Expenses** – Business expenses paid for with personal funds are reimbursements made to employees and same for owners, are not taxable income since these expenses were already paid by employee with their after-tax dollars, so these are just reimbursement.

- 3) **Distributions** – Distributions of company profits are normally paid after year end close when the company has finalized company financial statements for year and filed taxes. Distributions must be paid in proportion to % of ownership of an S Corporation, which might be 50/50, 60/40, 51/49% or whatever % split of ownership is stated in Articles of Incorporation when business was established or as later amended between the owners.

Distributions may be paid during the year, but at year end must be true up to these %. So whenever company funds are paid directly to owners or for their personal expenses, those amounts are counted as Distributions already paid to them for that fiscal year so would be deducted from their Distributions to be paid them at year end close true up. Distributions are profit earned and income subject to Federal and State income taxes.

- 4) **Imputed Income** – Certain expenses paid for S Corp owners by the business must also be counted as imputed income, for example, health insurance premium, company car, are most common (but see IRS website for full list). These expenses can be paid by the company and deducted as business expenses to reduce taxable income for a business, but must also be added to employee W-2 as “imputed income” and taxed accordingly. These expenses impact business and personal tax returns so your tax person handles but is your responsibility to make sure amount paid on books match amount on W-2’s.