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PAYING YOURSELF AS A FOUNDER

Owner draws, salaries, and a simple plan for paying yourself without starving the business.

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AT A GLANCE

- How you pay yourself depends on your business structure. Owners of sole proprietorships and most LLCs take **owner draws**. Owners of corporations, including LLCs taxed as S corporations, usually take a **salary** through payroll.
- Paying yourself something, even a little, on a regular schedule is healthier than taking money only when you're desperate.
- Always set money aside for **taxes** on what you earn.

WATCH OUT

Tax rules for owner pay are complex and depend on your structure and situation. Talk to a CPA or tax preparer before you set up how you're paid.

Why it matters

Many founders pay themselves nothing for too long, then burn out or quit. Others take whatever is in the account and leave the business short. A clear plan protects both you and the business. And lenders and investors want to see that the business can support its owner.

How it works

Structure	How owners are usually paid	Taxes
Sole proprietor	Owner draws	Owner pays income tax and self-employment tax on the business's profit, whether drawn or not
LLC (default tax treatment)	Owner draws	Same as sole proprietor, or as a partnership if there are several owners
LLC or corporation taxed as an S corporation	A reasonable salary through payroll, plus possible distributions	Payroll taxes on salary; income tax on profit
C corporation	Salary through payroll; profits may be paid as dividends	Company pays corporate tax; owner pays tax on salary and dividends

KEY POINT

For sole proprietors and most single-owner LLCs, you owe tax on the **profit**, not on what you take out. Taking less doesn't lower your tax bill.

A simple plan

1. **Know your numbers.** Check your monthly profit and cash flow. See **M-04 Reading a Profit and Loss Statement** and **M-06 Cash Flow: Why Profitable Businesses Still Run Out of Money**.
2. **Keep a cushion** of 1 to 3 months of business costs in the account first.
3. **Set a regular amount.** Pick a monthly pay you can count on, based on careful, not hopeful, profit.
4. **Set aside taxes.** Move a share of each payment, often 20% to 30%, into a tax savings account. Ask a tax preparer what fits.
5. **Review every 3 months.** Raise your pay as profit grows.

EXAMPLE

Rosa's cleaning company earns about $2,900 a month in profit before taxes. She keeps a $5,000 cushion in the business, pays herself **$2,000** on the 1st of every month, and moves **$600** into a tax savings account. The remaining $300 or so stays in the business to build its savings. When a new office contract added $800 a month in profit, she raised her pay to $2,500 after three steady months.

Common mistakes

- **Paying yourself nothing for years.** It's not sustainable, and it hides whether the business really works.
- **Taking money randomly.** It makes cash flow unpredictable.
- **Forgetting taxes.** Owners often owe quarterly estimated taxes. A surprise tax bill can sink a small business. See **M-13 Sales Tax, Payroll Tax and Staying Current**.
- **Not recording draws.** Every payment to yourself should be recorded in your books.

Your checklist

- ☐ Confirm how your business structure pays owners
- ☐ Ask a tax preparer about estimated taxes and owner pay
- ☐ Set your cushion target
- ☐ Choose a regular monthly pay amount and date
- ☐ Open a separate tax savings account
- ☐ Put a review every 3 months on your calendar

Key words, explained

Word	What it means
Owner draw	Money an owner takes from a sole proprietorship or LLC.
Salary	Regular pay through payroll, with taxes withheld.
Distribution	Profit paid out to owners, separate from salary.
Estimated taxes	Tax payments made during the year, often quarterly.
Reasonable salary	Pay for an S corporation owner that matches the work they do.

Where to go next

- **M-13 Sales Tax, Payroll Tax and Staying Current**
- **B-01 Choosing a Business Structure: Sole Proprietor, LLC or Corporation**
- **B-14 Business Taxes: What You Owe and When**

IMPORTANT
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