The Man's Take

Here's some guidance for small business owners on how much salary to take from their businesses.

In our role as accountants and trusted advisors for our small business clients, one of the most frequent questions we hear is, “How much salary should I take from my business?” The answer isn’t as simple as it seems. How much salary you take depends largely on your corporate entity structure.

Most limited liability companies (LLCs) and partnerships and all sole proprietorships are entities in which the net profits of the business flow directly to the owner of the business. This net profit is considered the business owner's salary, and is subject to all payroll taxes including FICA and Medicare tax. Although the net profit is considered salary, the business owner does not actually receive a W-2. The business owner must make quarterly estimated tax payments based on his or her projected share of the business income. We usually recommend setting aside approximately 35% to 40% of the salary for federal, state, and local estimated tax payments. Not paying the correct amounts could result in interest and penalties.

The S corporation owner is treated a little differently. Although considered an owner, he or she is also considered an employee for tax purposes. As an employee, the owner must receive a "reasonable" amount of salary and a W-2 at the end of the year, and not simply take all of his compensation in the form of a profit distribution. How much salary is reasonable is somewhat subjective.

The Internal Revenue Service (IRS) doesn't actually define what reasonable is; however, we have advised our clients to pay themselves a minimum salary of 30% to 40% of net profits. For example, if an S corporation has gross revenue of $150,000 and expenses of $50,000, the business owner should pay himself or herself a salary of at least $30,000 or $40,000, which is deducted against net profits. Our office has experienced an increase in S corporation audits in which the IRS is looking to see that a business owner is taking a reasonable amount of salary. The salary of the owner of a C corporation business is treated the same as that of any other employee: A W-2 is generated and all normal employment taxes are paid. As far as taxes are concerned, the owner’s salary can be set at any level.

When you're deciding on your salary, pay attention to the requirements of your business entity, and balance business and personal considerations with tax considerations.

By Steven Goldstein

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Bringing In More Revenue: The Role of Marketing Metrics

Are your firm's marketing efforts producing the results you want? The only way to find out is to measure the results of your firm’s marketing initiatives. A recent study challenges many professional services firms to establish measurements that truly assess the effectiveness of their programs.

In recent years, CPA firms have increasingly taken a structured approach to marketing their services. Many firms have increased their client base and revenues by tapping resources inside and outside the firm to expand their marketing efforts. Even so, many CPA firms and other professional services firms need to do more to improve their marketplace effectiveness to bring in more revenues. This is a conclusion of a study, "Increasing Marketing Effectiveness at Professional Firms," recently published by Concord, Massachusetts-based Expertise Marketing LLC and Glen Ellyn, Illinois-based Larry Bodine Marketing. Suzanne Lowe, president of Expertise Marketing and a professional services consultant, has over the years conducted several studies of professional services firms. The focus of each study was based on an advisory group’s request that certain issues be studied with the aim of helping firms market more effectively.

With this 2006 study, once again, Ms. Lowe and research partner Larry Bodine spotlight specific steps that will strengthen firms' efforts. The report focuses on the relationship between measurement and marketplace success. Firms need to ensure that their marketing and practice development efforts have been as effective as possible. To do so, they need to establish measurements that will tell them how well or poorly their marketing strategies are working.

To help professional services firms enhance their structure for improving marketing effectiveness, the report offers, along with commentary, "specific data about the highest ranked marketing and business development practices, the most effective measurement metrics, how firms monitor their effectiveness, how they perceive they're doing in measuring their marketing and business development initiatives, and how they overcome obstacles to measuring and improving their marketplace effectiveness.” The survey respondents included 127 marketing directors and 91 managing partners and CEOs. In addition to 72 CPA firm participants, the respondents represented law and engineering consulting firms.

The study results suggest that professional services firms are more than willing to extend their resources needed to achieve marketplace effectiveness. The results also suggest that a lack of marketing metrics hampers these firms in doing so. Among the study’s findings is that, although firms may be willing to spend money on marketing, they have spent “a paltry sum on measuring marketing—less than one-tenth of a percent—of an aggregate $94 billion in gross.” In a telephone interview, Ms. Lowe suggested that firms need to demonstrate their commitment to achieving marketplace effectiveness by formally budgeting funds for measuring this effectiveness.

"Most firms talk a good game about being better than their competitors,” Ms. Lowe said. “They may claim that they can exceed their competitors, but it’s mostly hot air if they don’t have a distinct process of measurement. The attitude of clients and prospective clients is ‘if you can’t prove to me that you’re superior, don’t tell me you are.’ Because proof is important to win clients, firms need to have an evaluation process in place. For example, they could demonstrate the results of their emphasis on professional qualifications and development to assure clients of receiving superior services.”

Self-delusion?
“Extremely effective” was the self-reported choice that 20% of respondents made about their effectiveness against rivals. But the report’s findings challenge professional services firms not to delude themselves that they are extremely effective against competitors just...
because they have some form of measurement program in place. In fact, some measurement programs have no teeth in them. The study found a statistical correlation between the level of self-reported competitive effectiveness and the use of what the study authors called ‘Client-Metrics’ -- measures that are “obvious, tangible, objective, and identified with clients.”

Along this line, the report concludes that “Benchmarking is not well-understood and is sparingly applied in professional services marketing. Benchmarking means setting a ‘highest achievable level of measurement’ and evaluating the firm’s progress toward attaining it.” The report contrasts benchmarking standards that are specific measurements and, therefore, would provide a meaningful assessment of progress with vague standards that lack tangible and objective measurements.

The contrast is demonstrated in the following list of measurements used by survey respondents:

**Examples of good benchmarking measurements**
- Average 9 proposals submitted per partner per year. Win 40% of all proposals. (Win 60% of those where we have a formal presentation of or meeting about the proposal.)
- We try to use the leader in our sector and our region in terms of market share as our benchmark. We try to replicate and perfect their strategies.
- Fifty percent increase in traffic from 2004.
- Want to win more than 30% of bids (industry average).
- 5% overall growth, with 25% margin at the manager level

**Examples of bad benchmarking measurements**
- Success in building a national brand will be our goal.
- We have no idea other than we hope the fees won are a multiple of the cost of the campaign.
- Maintain or improve turnover (revenue) rates from year to year.
- Higher revenues.
- Increase number of speaking engagements every year.

The full report discusses the importance of measuring marketplace effectiveness and how to measure real progress in the marketplace. To obtain the 80-page report, along with a 68-page case study, go to www.expertisemarketing.com/marketing_study_results.html.

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**Facing the Financial Future**

The findings of two recent polls conducted for the AICPA by Harris Interactive are perhaps not surprising. Still the findings can help CPA firms better serve their clients and employees.

A sharp contrast in how many Americans view their financial futures was revealed in two recent polls conducted by Harris Interactive for the AICPA. The polls offer CPAs insight into the thinking and behavior of clients and employees about how to prepare for a secure financial future. An issue that arises from both polls is awareness of what responsibility people must take for securing their financial future.

**Tough times ahead?**

"Many Americans are headed for tough retirement years and may not be able to maintain their current standard of living," concludes one AICPA/Harris poll. "A distressing gap exists between the public’s expectations for retirement and the reality," said Carl George, CPA, Chair of the AICPA’s National CPA Financial Literacy Commission and CEO of Clifton Gunderson LLP. "Moreover," he adds, "too many Americans think they can rely on the Social Security and pension safety net to carry them through."

George thinks Americans “must realize they have to take responsibility today for planning and saving for their retirement. Otherwise, they may find themselves working far longer than they anticipated or at a lower standard of living.”

Almost half of Americans (46%) expect to fund their retirement through Social Security and pensions, according to the poll, and an equal number expect that their retirement funds will last 10 to 20 years. Their expectations are unrealistic, says George. "If you plan for only 10 years, it’s likely you will outlive your savings. The fact is, Americans are living longer, and they should actually plan for 20 to 30 years, not 10 to 20."

Americans are also underestimating how much they will need to fund their retirement. More than a third of respondents, 39%, believe $500,000 will be sufficient. George noted, however, that, spread over 30 years, that amount becomes $16,000 a year, an amount that probably will be inadequate to cover such expenses as uninsured medical costs or assisted living.

The full report discusses the importance of measuring marketplace effectiveness and how to measure real progress in the marketplace. To obtain the 80-page report, along with a 68-page case study, go to www.expertisemarketing.com/marketing_study_results.html.