



Reasonable Compensation Simplified™

Reasonable Compensation for S Corps

Welcome to our webinar!



Thank You



Paul S. Hamann

Founder



Eric L. Green

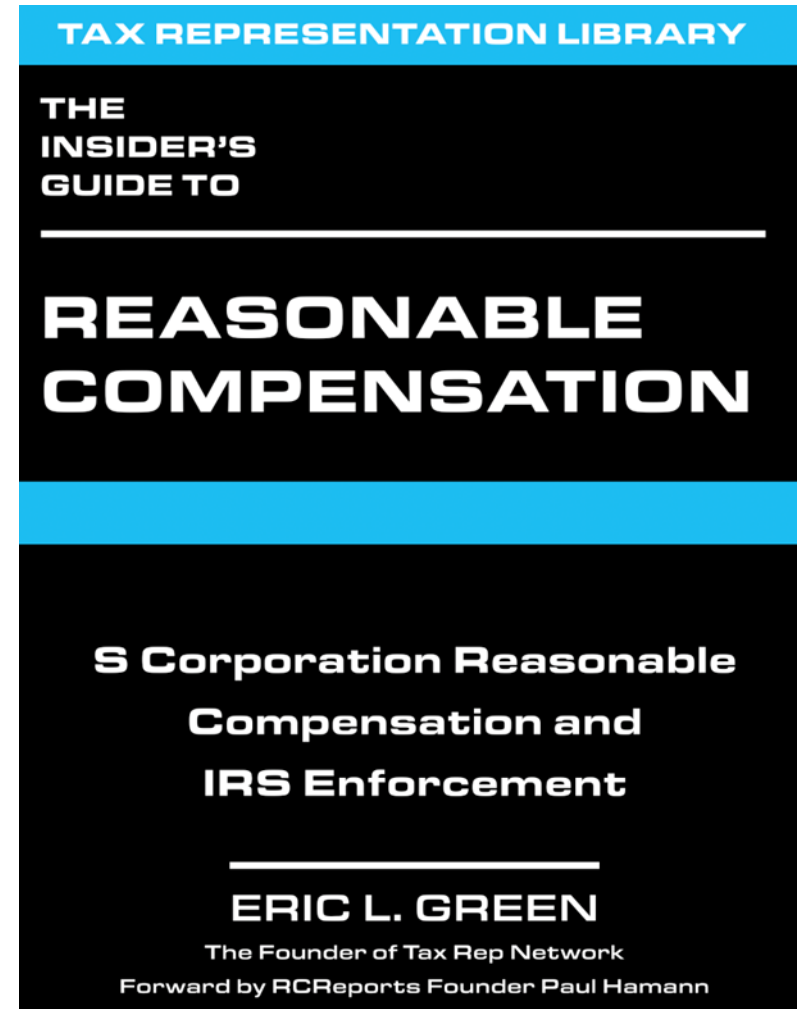
Founder of TRN

Housekeeping

- One ce/cpe credit
- Do at least 3 of the 4 attendance checks
- Look for a link to claim your certificate (EAs must provide their PTIN here)
- Issues? Email us at team@taxrepllc.com

Special Offer

- Get the Reasonable Comp Master Class (normally \$99) and the Insider's Guide to Reasonable Compensation (normally \$145) **for only \$149 (save \$100 today)**
- Use this link:
<https://tgpublish.com/reasonablecomp>
- Use this Promo Code: **REASONABLE50**



First Wave of the Tsunami is Here



Agenda

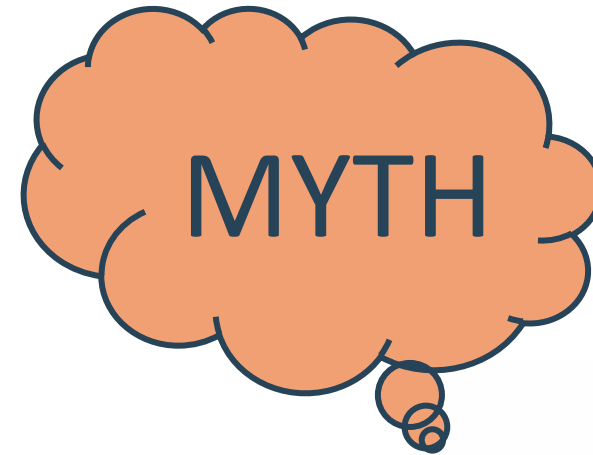
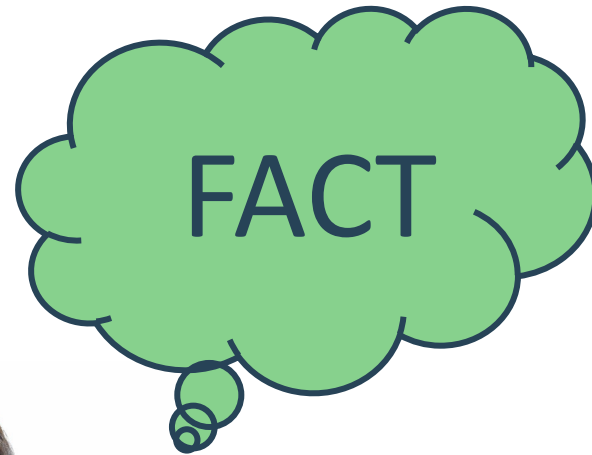
- Advantage Distribution V. Wages
- Reasonable Compensation in the courts
- IRS Guidelines
- Profitability V. Distributions
- Reasonable Compensation and the IRS
- Determining Reasonable Compensation
- Tips and Advice



Terms

- Reasonable Compensation = Replacement Cost 🚫🚫
- Reasonable Compensation = FMV Fair Market Value 🚫🚫
- Distributions = Dividends
- Distributions = Loan repayment, Return of basis
- Shareholder-employee (SE) = Corporate officer
- Shareholder-employee (SE) = S Corp owner

Reasonable Compensation for S Corps



Polling Question #1

Which of the following methods of determining Reasonable Compensation are recognized by the IRS:

- A. Industry Rule (Set wages as a percentage of sales or revenue based on industry standards)
- B. 50/50 Rule (50% distribution – 50% Wages)
- C. Safe Harbor Rule (Set wages at the S.S. Max)
- D. All the above
- E. None of the above

Polling Question #1

Which of the following methods of determining Reasonable Compensation are recognized by the IRS:

- A. Industry Rule (Set wages as a percentage of sales or revenue based on industry standards)
- B. 50/50 Rule (50% distribution – 50% Wages)
- C. Safe Harbor Rule (Set wages at the S.S. Max)
- D. All the above
- E. **None of the above**

In the last year, we've asked
100,000+ Tax Advisors
this question.



73% believe at least one myth.



Myth:

60/40 Rule or 50/50 Rule

"The 60/40 rule is a simple approach that helps S corporation owners determine a reasonable salary for themselves. Using this formula, they divide their business income into two parts, with 60% designated as salary and 40% paid as shareholder distributions."



Myth:

Industry Rule

Set wages as a percentage of sales or revenue based on industry standards | Payroll as a percentage of Net-Income

"That reasonable salary can be anywhere from 30-50% of the net income from your business."



edwardcollins_upleveled
Edward Collins · 2023-9-6

Myth:

Safe Harbor Rule

Set wages at the Social Security maximum limit

Myth:

Wild A** Guess

"Save employment taxes by setting up your consulting business as an S-Corp. At the lower end you get to decide a fair wage to pay yourself and save social security taxes."



markjkohler
Mark J. Kohler · 2023-11-11

Reasonable Compensation for S Corps



Distribution vs Wages/Salary

Wages/Salary
=
Payroll Taxes

Distributions
≠
Payroll Taxes

Substantial Services
=
Reasonable Compensation

Distribution V. Wages/Salary

Example 1

- Scott Stone 100% of Stone Concrete (S Corp)
- Full Time Employee of Stone Concrete
- \$100,000 income before considering Scott's salary
- Scott takes a \$100,000 salary = taxable income is zero
- \$100,000 wages \longrightarrow 1040



Distribution V. Wages/Salary

Example 1 (Continued)

- Scott and Stone Concrete responsible for Payroll Taxes
 - 7.65% Stone Concrete SS/Medicare = \$7,650
 - 7.65% Scott Stone SS/Medicare = \$7,650
 - State & Federal Unemployment Tax = ???
- **Total Tax Liability** **\$15,300+**

Distribution V. Wages/Salary

Example 2

- Scott Stone 100% of Stone Concrete (S Corp)
- Full Time Employee of Stone Concrete
- \$100,000 income before considering Scott's salary
- Scott takes a \$100,000 distribution
- \$100,000 income \longrightarrow 1040



Distribution V. Wages/Salary

Example 2 (Continued)

- Scott and Stone Concrete Payroll Taxes = \$0.00
- Self Employment Tax = \$0.00
- Income Tax (return of basis) = \$0.00
- Total Tax Liability = \$0.00

Net tax savings \$15,300+



Distribution V. Wages/Salary

Wages/Salary



vs

Distributions



IRS Requirement

“ Distributions and other payments by an S corporation to a corporate officer must be treated as wages to the extent the amounts are reasonable compensation for services rendered to the corporation.

~ Instructions 1120S

Polling Question #2

Reasonable Compensation in Courts

IRS 25-1*



VS



*Davis v. U.S.

Reasonable Compensation in Courts

DAVID E. WATSON, P.C., V. UNITED STATES OF AMERICA
(2010)



VS



Reasonable Compensation in Courts

Low Salary V. Profit Distributions

- 2002 Profit Distributions = \$203,651
- 2002 Salary = \$24,000
- 2003 Profit Distributions = \$175,470
- 2003 Salary = \$24,000

Reasonable Compensation in Courts

IRS Objected

- Education:
 - Graduate Degree
- Experience:
 - 20 Years
- Time: Full Time
 - (35-45 hours per week)



Reasonable Compensation in Courts

IRS Audit 2007



Reasonable Compensation in Courts

Reasonable Compensation

\$91,044 for 2002

\$91,044 for 2003

Reasonable Compensation in Courts

	2002	2003
Reasonable Compensation	\$91,044	\$91,044
Actual Salary Paid	<u>\$24,000</u>	<u>\$24,000</u>
<u>Re-Characterized</u>	\$67,044	\$67,044

Total Re-Characterization = \$134,088

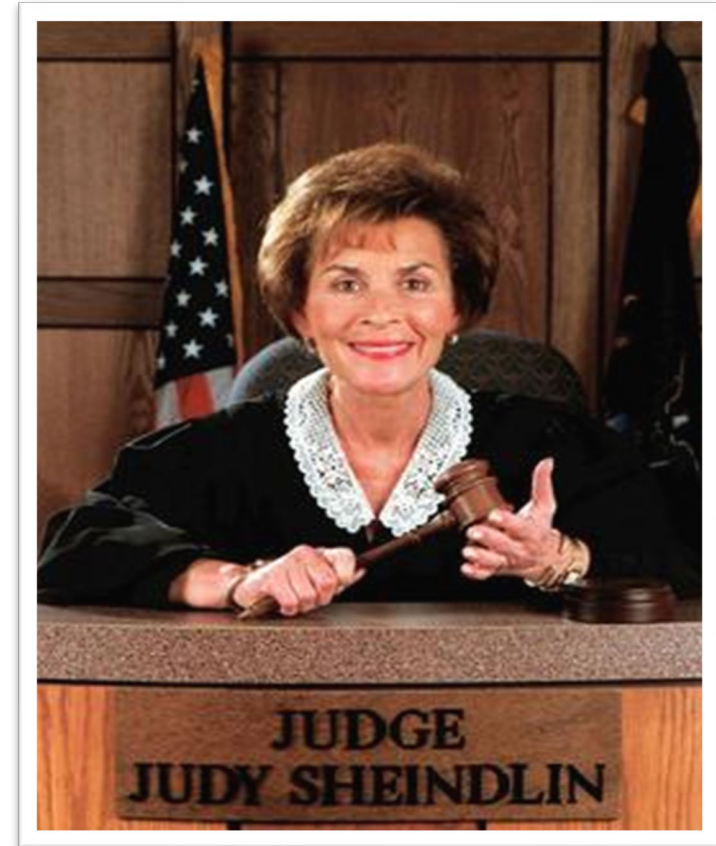
Reasonable Compensation in Courts

\$48,521

\$20,000

Reasonable Compensation in Courts

Watson V. IRS



Reasonable Compensation in Courts

Ruling in favor of IRS 2010



VS



Reasonable Compensation in Courts

IRS

- Graduate Degree
- 20 Years experience
- Full Time employee

Various Job Duties:



- CPA/Accountant
- Partner
- Re-structured businesses

No Research and No Documentation

Reasonable Compensation in Courts

Appealed



Reasonable Compensation in Courts

Upheld District Courts Ruling 2012



VS



Reasonable Compensation in Courts

Appealed Denied



Take Aways

- Paid Some RC
- IRS did not recharacterize all distributions
- Single Shareholder
- Services only

Reasonable Compensation in Courts

SEAN MCALARY LTD, INC. v. COMMISSIONER (IRS) (2013)



VS



Reasonable Compensation in Courts

McAlary Ltd = Real Estate Company

- 2006 Net Income = \$231,454
- 2006 Distribution = \$240,000
- 2006 Salary = Zero



Reasonable Compensation in Courts

IRS Calculation: \$100,755

- Primary Job Function – Real Estate Broker
- Full Time (12 hour days 6-7 days per week)
- Compared McAlary LTD performance with peers in the real estate industry 🚫

Reasonable Compensation in Courts

IRS Calculation: \$100,755

- **Replacement Cost** – McAlary LTD could expect to pay \$48.44/hour to another individual in exchange for the services Mr. McAlary performed 
- **Fair Market Value** – \$100,755 would be FMV of the services Mr. McAlary performed for his S Corp 

Reasonable Compensation in Courts

IRS Calculation: \$100,755 = \$48.44 x 2,080

- The Bureau of Labor Statistics defines Year-Round, Full-Time employment as **2,080** hours per year.
- 40 Hour Work Week x 52 Weeks/Year
- McAlary often worked 12-hour days with few days off

Reasonable Compensation in Courts


McAlary Calculation: \$24,000

- Compensation Agreement 🚫
- BOD Meeting Minutes 04-01-2004
- Increases Based on Number of Agents

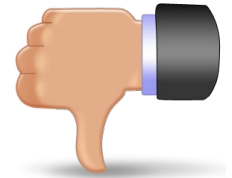


Reasonable Compensation in Courts



Court Calculation: \$83,200

- Various Services 
- Wage Range
- Hourly Wage = \$40.00
- $2,080 \times \$40.00 = \$83,200$

Reasonable Compensation in Courts





Court Calculation: \$83,200 = 2,080 x \$40.00

- **Compensation Agreement** – “We are not persuaded that the remuneration agreement represents a sound measure of the value of the services that Mr. McAlary provided ... The agreement clearly was not the product of an arm's-length negotiation.” 
- **Industry Comparison** – “(IRS Expert) did not explain how a *comparison of compensation measured as a percentage of gross receipts with compensation measured as a percentage of net sales* would aid the Court ... In the end, we do not find this portion of (the experts) report to be persuasive or helpful.” 

Reasonable Compensation in Courts




Court Calculation: \$83,200 = 2,080 x \$40.00

- **Compensation Agreement** – “We are not persuaded that the remuneration agreement represents a sound measure of the value of the services that Mr. McAlary provided ... The agreement clearly was not the product of an arm's-length negotiation.” 
- **Industry Comparison** – “(IRS Expert) did not explain how a *comparison of compensation measured as a percentage of gross receipts with compensation measured as a percentage of net sales* would aid the Court ... In the end, we do not find this portion of (the experts) report to be persuasive or helpful.” 

Reasonable Compensation in Courts



Court Calculation: \$83,200 = 2,080 x \$40.00

- **Various Services** – Management; Supervision; Recruiting; Sales; Advertising; Purchasing; Bookkeeper; Record Keeping... 
- **Experience** – Low; New to the Industry
- **COESS-BLS** – Range \$32.99 to \$64.28

“ Determining an employee's reasonable compensation is dependent upon a number of factors and is far from an exact science.

Reasonable Compensation in Courts

Court Rulings

- Sean McAlary Ltd, Inc. v. Commissioner 2013
- Glass Blocks Unlimited v. Commissioner 2013
- Patrick & Suzanne Herbert v. Commissioner 2012
- David E. Watson, P.C. v. United States 2010
- JD & Associates, LTD v. United States 2006
- Joseph M. Grey Public Accountant, P.C. v. Commissioner 2002**
- Veterinary Surgical Consultants, P.C. v. Commissioner 2003**
- Joly v. Commissioner 2000
- Spicer Accounting, Inc. v. United States 1990
- Joseph Radtke, S.C. v. United States, 1989

Cases in orange are accounting firms
** Clients of Joseph M. Gray

Polling Question #3

Definition, IRS

“ Reasonable compensation is the value that would ordinarily be paid for like services by like enterprises under like circumstances

~ IRS Code: Section 162-7(b)(3)

“ Reasonable & Services Rendered

~IRS Code 162(a)(1)

- Replacement Cost
- Fair Market Value




IRS Guidelines

Notice of Acceptance as an S Corporation

We would also like to take this opportunity to inform you of your tax obligations related to the payment of compensation to shareholder-employees of S corporations.

When a shareholder-employee of an S Corporation provides services to the S corporation, reasonable compensation generally needs to be paid. This compensation is subject to employment taxes.

 Tax practitioners and subchapter S shareholders need to be aware that **Revenue Ruling 74-44** states that the Internal Revenue Service (IRS) will re-characterize small business corporation dividends paid to shareholders as salary when such dividends are paid to the shareholders in lieu of reasonable compensation for services.

This position has been supported in several recent court decisions.

IRS Guidelines

W-2 or 1099

- Revenue Ruling 74-44; IRC § states:
 - An officer of a corporation is considered an **EMPLOYEE**
- Employee or Independent Contractor
 - Under common-law rules, anyone who performs services for you is your employee *if you can control what will be done and how it will be done*

1099

W-2

IRS Guidelines

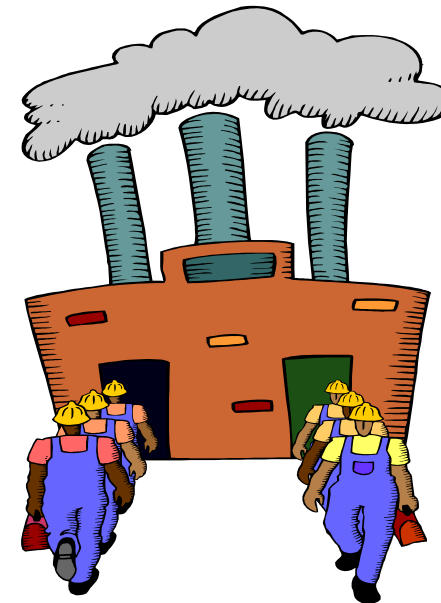
The key to establishing reasonable compensation is determining what the shareholder-employee did for the S corporation

1. Services of non-shareholder employees
2. Capital and equipment
3. Services of shareholders



IRS Guidelines

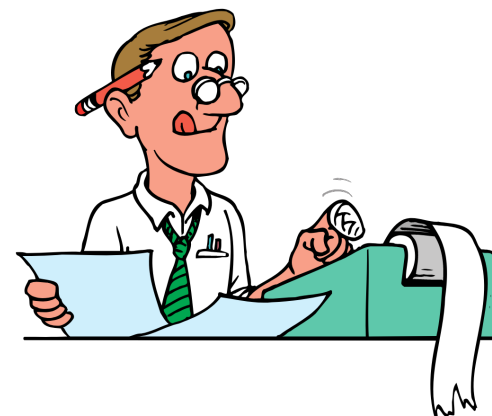
Services of non-shareholder employees, or Capital & equipment



IRS Guidelines

Services of shareholder

In addition to the shareholder-employee direct generation of gross receipts, the shareholder-employee should also be compensated for administrative work performed !



IRS Guidelines




Wage Compensation for S Corporation Officers

FS-2008-25, August 2008

Corporate officers are specifically included within the definition of employee for FICA (Federal Insurance Contributions Act), FUTA (Federal Unemployment Tax Act) and federal income tax withholding under the Internal Revenue Code. When corporate officers perform services for the corporation, and receive or are entitled to receive payments, their compensation is generally considered wages. Subchapter S corporations should treat payments for services to officers as wages and not as distributions of cash and property or loans to shareholders.

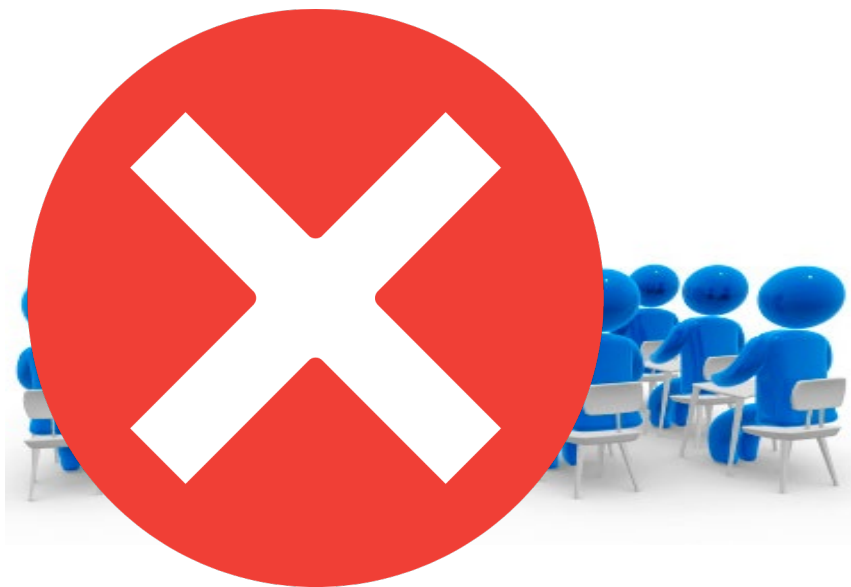
IRS Guidelines

Some factors considered by the courts in determining reasonable compensation:

- 1 • Training and experience
- 2 • Duties and responsibilities
- 3 • Time and effort devoted to the business
 - Dividend history
 - Payments to non-shareholder employees
- Timing and manner of paying bonuses to key people
- What comparable businesses pay for similar services
- Compensation agreements 
- The use of a formula to determine compensation

IRS Guidelines

1. Training and experience



&



IRS Guidelines

2. Duties and responsibilities



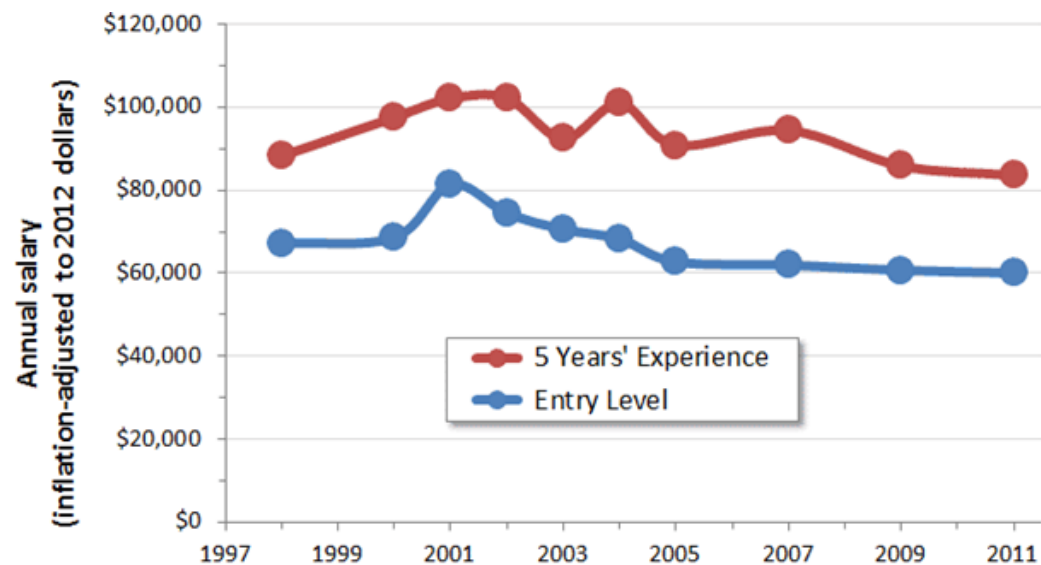
IRS Guidelines

3. Time and effort devoted to the business



IRS Guidelines

4. What comparable businesses pay for similar services

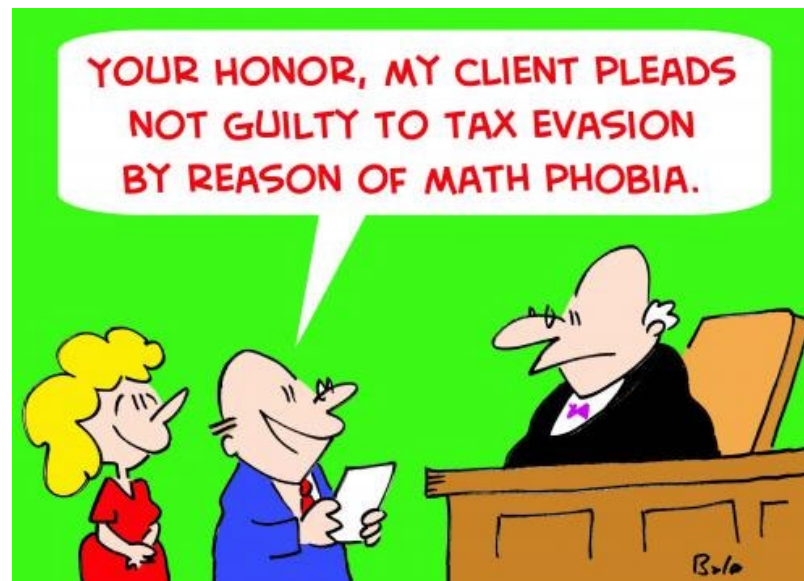


IRS Guidelines

5. The use of a formula to determine compensation



© Mary Anne Lloyd/Laughing Stock



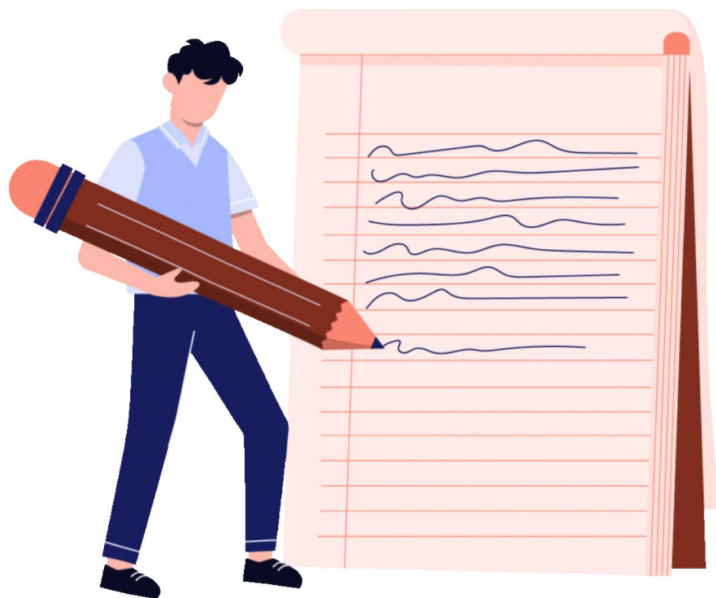
IRS Guidelines

6. Payments to non-shareholder employees



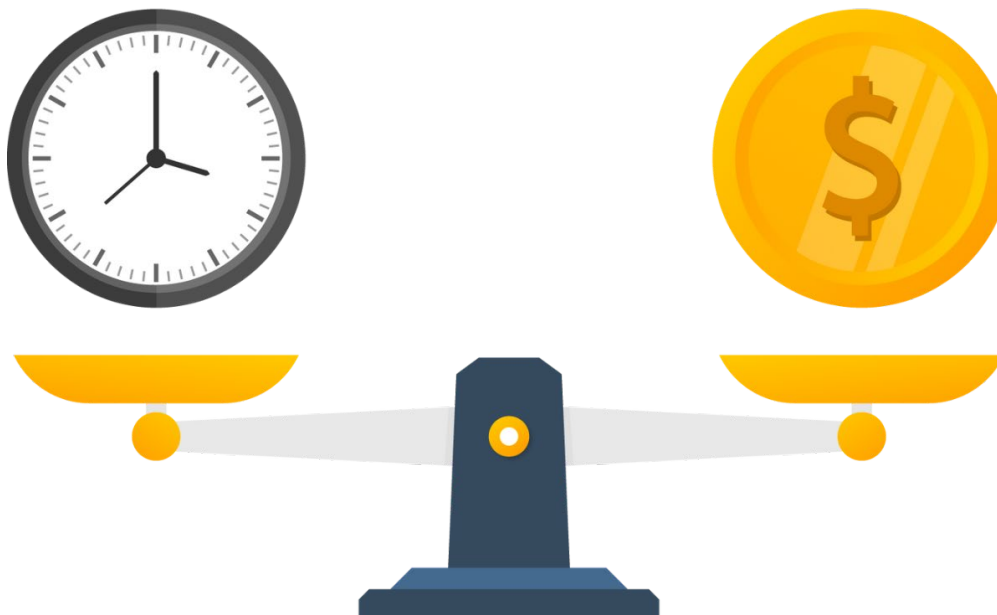
IRS Guidelines

7. Compensation agreements



IRS Guidelines

8. Timing and manner of paying bonuses to key people



IRS Guidelines

9. Dividend history



Polling Question #4

Profitability v. Distributions

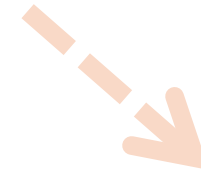


Profitability v. Distributions

Reasonable Compensation



Distributions



Profitability

“ The amount of reasonable compensation will never exceed the amount received by the shareholder either directly or indirectly.

~ FS-2008-25

Profitability v. Distributions

Example 1

- Scott Stone 100% of Stone Concrete (S Corp)
- Scott's RC figure = \$68,788
- Stone Concrete Net Profit = \$210,000
- Scott takes \$200,000 out of Stone Concrete
- Scott receives wages (RC) of \$68,788
- Scott receives a distribution of \$131,212
\$200,000

Profitability v. Distributions

Example 2

- Scott Stone 100% of Stone Concrete (S Corp)
- Scott's RC figure = \$68,788
- Stone Concrete Net Profit = \$23,000
- Scott takes \$30,000 out of Stone Concrete
- Scott receives wages (RC) of \$30,000
- Scott receives a distribution of \$ 0
\$30,000

Profitability v. Distributions

Example 3

- Scott Stone 100% of Stone Concrete (S Corp)
- Scott's RC figure = \$68,788
- Stone Concrete Net Profit = \$150,000
- Scott takes \$0 out of Stone Concrete
- Scott receives wages (RC) of \$0
- Scott receives a distribution of \$0
\$0

Profitability v. Distributions

Example 4

	Year 1	Year 2	Year 3	Total
Scott RC	\$70k	\$70k	\$70k	\$210k
Net Profit	\$150k	\$175k	\$200k	\$525k
Scott Takes	\$0	\$0	\$500k	
Wages	\$0	\$0	\$210k	
Distribution	\$0	\$0	\$290k	

Profitability v. Distributions

Payroll Tax Savings – Example 4

	Year 1	Year 2	Year 3		Years 1-3
Reasonable Compensation	\$70,000	\$70,000	\$70,000		\$210,000
FICA 12.4% (2024 limit 168,600)	\$8,680	\$8,680	\$8,680		\$20,906
Medicare 2.9% (all)	\$2,030	\$2,030	\$2,030		\$6,090
Medicare Surtax 0.9% (over \$200K)	\$0	\$0	\$0		\$90
	\$10,710	\$10,710	\$10,710		\$27,086
			Total	\$32,130	
				-\$27,086	
			Tax Savings	\$5,044	

Polling Question #5

Shareholder Loan or Capital Contribution

GLASS BLOCKS UNLIMITED v. COMMISSIONER (IRS) (2013)



VS



How an S Corp can Lose Money and Still be Required to Pay
Reasonable Compensation

Shareholder Loan or Capital Contribution

Glass Blocks Unlimited – Fredrick Blodgett

- 2007 Net Income = \$877
- 2007 Transferred in = \$45,000
- 2007 Transferred out = \$30,844
- 2007 Salary = Zero



Shareholder Loan or Capital Contribution

IRS Position

- Transfer in was a contribution to capital (basis)
- Transfer out was a distribution (Return of basis)
- Reasonable Compensation must be paid before a distribution can be made

Shareholder Loan or Capital Contribution

Glass Blocks Position

- Transfer in was a shareholder loan to GBU
- Transfer out was a repayment of the shareholder loan
- Reasonable Compensation does not apply

Shareholder Loan or Capital Contribution

Court Finding

Transfers in question were capital contributions and not bona fide loans

- No Written Agreements or Promissory notes
- No interest charged
- No security (collateral)
- No fixed repayment schedule

example
Promissory Note
I, Local Boy, do promise to pay
Aunty Mele, the sum of \$ 10,000.
Repayment to be made in the
form of 200 equal payments at
5%, payable on the 1st of each
month, starting 8/1/2012, until
the total debt is satisfied. Signed
Local Boy
7/1/2012

Shareholder Loan or Capital Contribution

Court Finding

“ Where the expectation of repayment depends solely on the success of the borrower's business, rather than on an unconditional obligation to repay, the transaction has the appearance of a capital contribution.

Shareholder Loan or Capital Contribution

Math

- Net Income (before) \$877
- Wages **\$-30,844**
- Employment Taxes **\$-2,360**
- Penalty & Interest **\$-1,923**
- 2007 Net Loss (after) **\$-34,250**

Did the IRS Really Lose?

DAVIS v. UNITED STATES (1994)



VS



Did the IRS Really Lose?

DAVIS v. UNITED STATES

Mile High Calcium Owned by:

- Carol L. Davis
- Henry Adams (husband)
- Transfers In and Out 1987-1989
- Assessed Taxes + Interest & Penalties of \$39,220

Did the IRS Really Lose?

DAVIS v. UNITED STATES

Henry Adams – President

- Not an Employee
- No Active Participation
- Worked for outside employers
- Officer in name only
- There is an exception for officers who perform only minor services... (Treas. Reg. § 31.3121(d)-(1)(b))

Did the IRS Really Lose?

DAVIS v. UNITED STATES

Carol L. Davis

- Was an Employee
- 12 hours per month (2.77 per week)
- \$8.00 per hour
- ~~\$39,220~~.....\$647

Reasonable Compensation & the IRS

Form 1125-E

- 2011 Required for Gross Revenue 500k+
 - Collecting data for future comparisons

- Disclosure Standards

- Dollar Amounts must be verifiable
- Taxpayer must be able to demonstrate the origin of the amount claimed
- Taxpayer must be able to show he entered the amount in good faith

Form 1125-E only if total receipts are \$500,000 or more. See instructions for definition of total receipts.

(a) Name of officer	(b) Social security number (see instructions)	(c) Percent of time devoted to business	Percent of stock owned		(f) Amount of compensation
			(d) Common	(e) Preferred	
		%	%	%	
		%	%	%	

Polling Question #6

Reasonable Compensation & the IRS

Pre 2005...

- Joly v. Commissioner 2000
 - **Established authority to reclassify distributions as wages**
- Veterinary Surgical Consultants, P.C. vs. Commissioner 2001
- Joseph M. Grey Public Accountant, P.C. 2002
 - **Reinforced employment status of shareholders as employees**
- TIGTA 7-2002
 - **The IRS does not always address S Corp officer compensation during examination**
 - **Average W-2 Wages \$5,300**
 - **Average Distribution \$349,323**

Reasonable Compensation & the IRS

IRS Launches Study of S Corporation Reporting Compliance



IR-2005-76, July 25, 2005

WASHINGTON — Internal Revenue Service officials announced today the launch of a study to assess the reporting compliance of S corporations. The study, carried out under the National Research Program (NRP), will examine 5,000 randomly selected S corporation returns from tax years 2003 and 2004.

Reasonable Compensation & the IRS

GAO December 2009

Actions Needed to Address Noncompliance with S Corporation Tax Rules

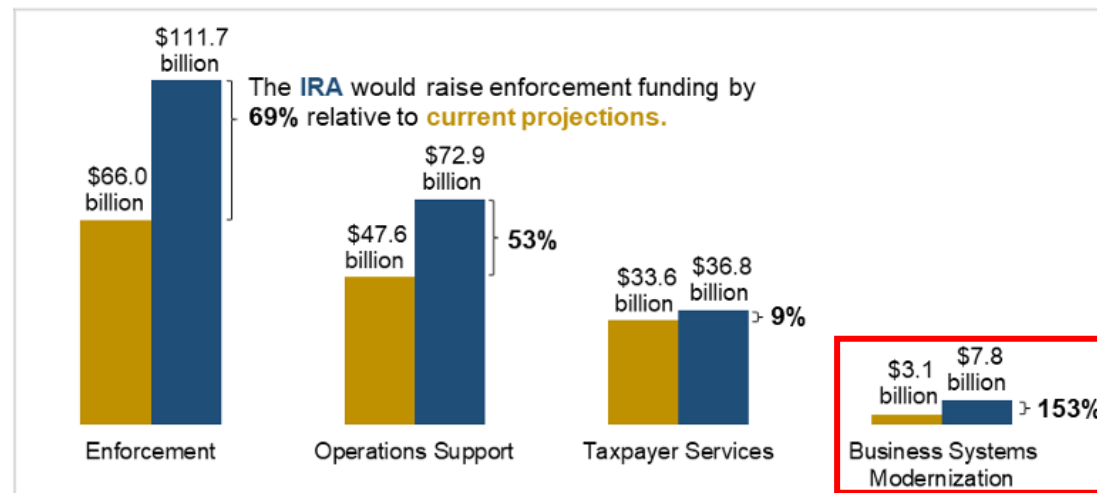
- GAO calculated that in the 2003 and 2004 tax years, the net shareholder compensation underreporting equaled roughly **\$23.6 billion**
- Further analyze the extent of noncompliance involving a long standing concern over inadequate shareholder compensation, and identify options for improving compliance (**PROBLEM**)
- Improve guidance to IRS examiners so that they might better target and determine adequate shareholder compensation (**TRAINING & TOOLS**)

Reasonable Compensation & the IRS

Inflation Reduction Act of 2022 (IRA22)

- IRS Funding: \$80 Billion – \$45.6 Billion for Enforcement
- 87,000 new agents?
- **Massive Investment in Technologies that aid Investigations - \$4.7 Billion**

Figure 1. The IRS's Budget Authority Through FY2031 Under the Inflation Reduction Act



Source: Congressional Budget Office; Part 3 of Title I, Subtitle A of the Inflation Reduction Act.

Note: Assumes no change in base appropriations.

Reasonable Compensation & the IRS

2023 PayrollOrg* Congress

Identified reasonable compensation audits as an area the IRS will focus on in the immediate future.

SB/SE will be focusing on: Payroll Compliance [940 & 941]

- ERC Fraud Initiative: [56 hours of training]
- S Corp Audits: Assessing if S Corp owners receive RC
- Worker Classification Audits: 1099 v. W-2



Paul Mamo

Assistant Deputy Commissioner for Services & Enforcement



Dan Lauer

Director of SB/SE, Examinations and Specialty Tax

*Formerly The American Payroll Association & Global Payroll Management Institute

Reasonable Compensation & the IRS

Challenges are coming from multiple sources [BTW]

- Traditional 1120S Audits
- Compliance Initiative Projects
- Payroll / 1099 / 941 Audits*
- ERC Audits
- Lifestyle Audits*
- State Level

*Preparer Penalties

Reasonable Compensation & the IRS

Preparer Penalties \$5,000 IRC sec. 6694(b)

- IRS does expect preparers to have appropriate checklists
- IRS does not expect the preparer to merely accept the information
- IRS does require the preparer to be proactive
- Penalties can and will be imposed on preparers



Reasonable Compensation & the IRS

Burden of Proof IRC sec. 7491

- RC Challenged → the taxpayer has the “Burden of Proof”
- Burden of Proof shifts to the IRS if:
 - Taxpayer introduces Credible Evidence
 - Taxpayer has kept Records that meet IRS requirements

“We have provided RCReports to IRS auditors without issues or problems when asked as a checklist item on a small business audit.”

~Randy Tarpey, CPA



Death by Preparer Penalty

What about Bob...

The Danger of Ignoring Reasonable Compensation?

- Client gets hit with an adjustment
- Client blames you
- IRS goes after you the preparer



Reasonable Compensation & the IRS

No Tax Court for Reasonable Compensation 2017

Notice of Employment Tax Determination under IRC §7436 - Additional Compensation to Officer Employees

- Not Issue Letter 3523: Notice of Determination of Worker Classification
 - Cannot proceed to Tax Court
 - Pay Tax
 - Sue for refund

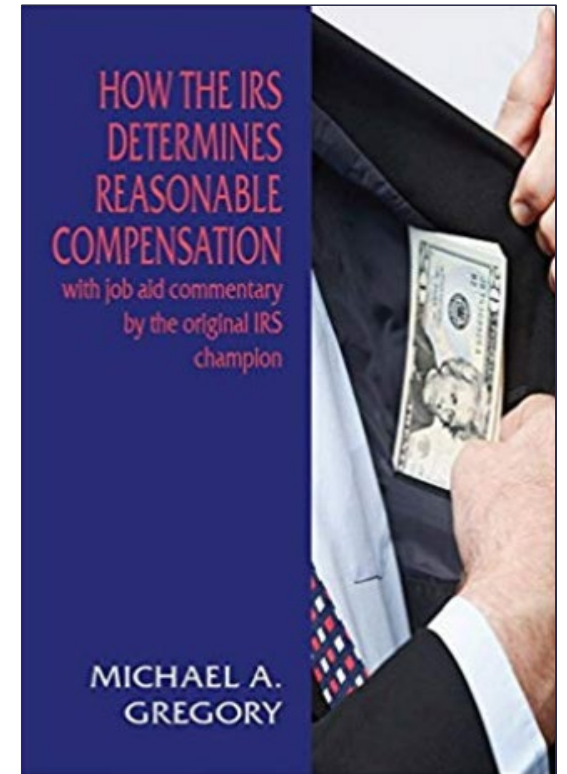


Polling Question #7

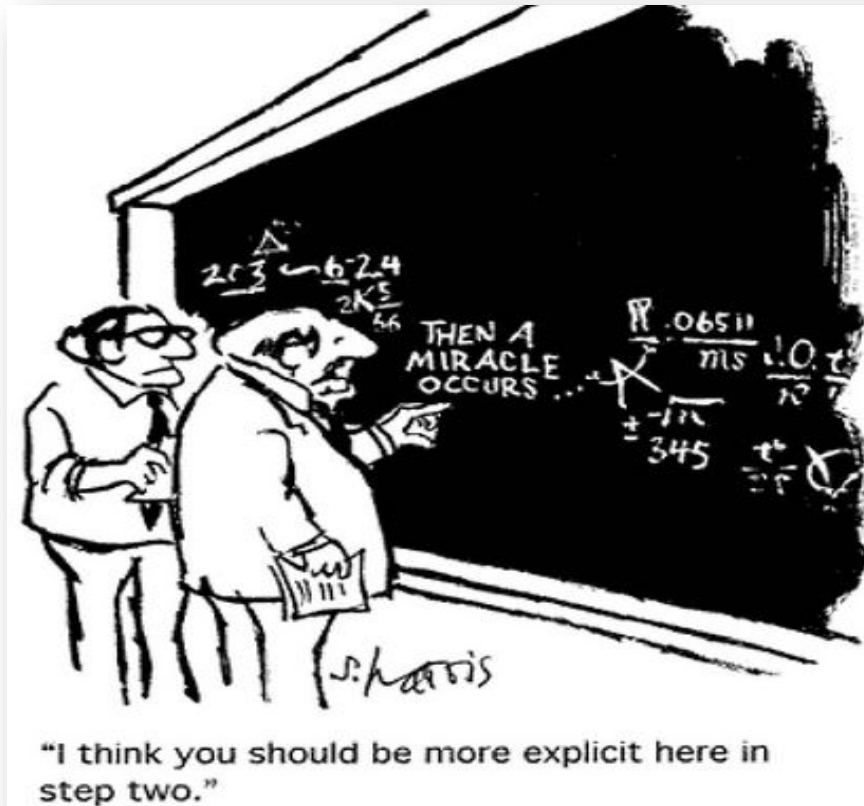
Determining Reasonable Compensation

Reasonable Compensation Job Aid for IRS Valuation Professionals

- Companies have the burden of showing that compensation is reasonable
- Three Approaches
- Michael A. Gregory CVA, CBA, ASA



Determining Reasonable Compensation



Reasonable Compensation

Job Aid for IRS Valuation Professionals*

*(This Job Aid Can Also be Helpful to Revenue Agents and Other IRS Field Personnel)

October 29, 2014

How – Cost Approach

AKA Many Hats Approach



	D	E	F	G
Materials Cost Estimate Luis Cedillo per#6				
Size/Description	Quantity	Unit Cost	Cost	
Cubic yard	2.5	\$75.00	\$187.50	
#4 (1/2in. X 10ft)	20	\$4.47	\$89.40	
2in. x 4in. - 12ft	2	\$11.31	\$22.62	
2in. x 4in. - 16ft	2	\$14.95	\$29.90	
2in. x 4in. - 92 5/8in.	45	\$3.10	\$139.50	
2in. x 4in. - 8ft	16	\$3.06	\$48.96	
2in. x 4in. - 8ft	15	\$3.06	\$45.90	
2in. x 4in. - 8ft	8	\$3.06	\$24.48	
2in. x 6in. - 8ft	6	\$4.20	\$25.20	
1/2in. x 4ft x 8ft sheet	15	\$6.85	\$102.75	
8ft x 150ft	1	\$98.00	\$98.00	
Bundle of 200 sq. ft	3	\$300.00	\$900.00	
1/2in. x 4ft x 8ft sheet	15	\$6.85	\$102.75	
Gallon (400 sq. ft per gallon) 2 coats	3	\$15.99	\$47.97	
3.5in. x 15in. - 40 sq. ft	3	\$8.48	\$25.44	
1/2in. 2 x 6in.	14	\$0.42	\$5.88	
24in. x 36in.	2	\$134.00	\$268.00	
Double - 7ft x 80in.	1	\$250.00	\$250.00	

How – Cost Approach

- All Tasks Performed
- Apportion Time
- Skill-Proficiency
- Comparability Data
- Small Business



"The consultant said I was wearing too many hats."

Scott Stone at 25

Your Interview

You have specified **40 hours** as the amount of time you work per week.

You have specified **Cook County, Illinois** as primary location of work.

Time & Proficiency Allocation

You perform **Sales Representative** duties for **4.0** hours per week with **Below Average** proficiency.

You perform **Bookkeeper** duties for **4.0** hours per week with **Below Average** proficiency.

You perform **Purchasing Clerk** duties for **2.0** hours per week with **Average** proficiency.

You perform **Business Office Manager** duties for **6.0** hours per week with **Average** proficiency.

You perform **Concrete Finisher** duties for **12.0** hours per week with **Above Average** proficiency.

You perform **Maintenance Mechanic** duties for **12.0** hours per week with **Above Average** proficiency.



Scott Stone at 25



Page 1 of 7

Report for Scott Stone of Stone Concrete, Inc.

Your estimated annual Reasonable Compensation: **\$68,788**

Thank you for entrusting Sam Miller of Potomac Tax and Valuation, PC with your Reasonable Compensation analysis. This report provides a reasonable estimate of the value of services rendered to your S Corporation based on your responsibilities and the duties that you perform annually. Reasonable Compensation is defined by the IRS as "The value that would ordinarily be paid for like services by like enterprises under like circumstances".

The calculated salary is determined by the reasonable compensation based on the type of work performed, the skill set performed and the number of hours the work is performed annually. You told us that you work 2080 hours per year. This analysis indicates the annual salary of \$68,788 would be a reasonable cost to hire someone with the duties and responsibilities that you currently perform.

Potomac Tax and Valuation, PC recommends completing a reasonable compensation report annually.

Reasonable Compensation Figure

Details the salary range for the owner's industry and location and provides a suggested reasonable compensation figure.

Compensation Details

Detailed breakdown of the compensation tied to each task that the owner performs.

Task Category

Categories of tasks completed by the owner.

Standard Tasks & Proficiency

Tasks commonly associated with running a small business and the Owner's proficiency level for this specific task.

My Business Tasks

Specialized tasks the owner performs for their business that fall outside of standard business tasks.

Your Time

Breakdown of how the owner spends their time in the business. This information is based on the interview completed.

Your Compensation

How the compensation number is affected by each task the owner performs.

My Business

60% of your time

1,248 hours per year

66.85% of your comp.

Task	Proficiency	Category	Overall	Hours	Wage	Annual
Concrete Finisher	Above Avg	50%	30%	624.0	\$45.21	\$28,211
Maintenance Mechanic	Above Avg	50%	30%	624.0	\$28.48%	\$17,772

Page 2 of 7

Report for Scott Stone of Stone Concrete, Inc.

Task	Proficiency	Category	Overall	Hours	Wage	Annual
Advertising - Sales - Marketing						
			10% of your time	208 hours per year	6.4% of your comp.	
Sales Representatives	Below Avg	100%	10%	208.0	\$21.18	\$4,405
Accounting - Finance - Bookkeeping						
			10% of your time	208 hours per year	4.99% of your comp.	
Bookkeeper	Below Avg	100%	10%	208.0	\$16.16	\$3,361
Purchasing - Inventory - Shipping - Receiving						
			5% of your time	104 hours per year	3.57% of your comp.	
Purchasing Clerk	Average	100%	5%	104.0	\$23.61	\$2,455
Management - Supervision						
			15% of your time	312 hours per year	18.29% of your comp.	
Business Office Manager	Average	100%	15%	312.0	\$40.33	\$12,563
My Business						
			60% of your time	1,248 hours per year	66.85% of your comp.	

Your Interview

You have specified **40 hours** as the amount of time you work per week.
 You have specified **Cook County, Illinois** as primary location of work.

Time & Proficiency Allocation

- You perform **Sales Representative** duties for **4.0** hours per week with **Below Average** proficiency.
- You perform **Bookkeeper** duties for **4.0** hours per week with **Below Average** proficiency.
- You perform **Purchasing Clerk** duties for **2.0** hours per week with **Average** proficiency.
- You perform **Business Office Manager** duties for **6.0** hours per week with **Average** proficiency.
- You perform **Concrete Finisher** duties for **12.0** hours per week with **Above Average** proficiency.
- You perform **Maintenance Mechanic** duties for **12.0** hours per week with **Above Average** proficiency.

Percentage of Time & Annual Hours

Annual percentage of owner's time spent on that task and hours per year the owner spends on this task.

Hourly Wage & Annual Compensation

Hourly wage for this task based on location and proficiency and hourly wage x annual hours worked for that task.

How – Market Approach

AKA Industry Comparison Approach



How – Market Approach

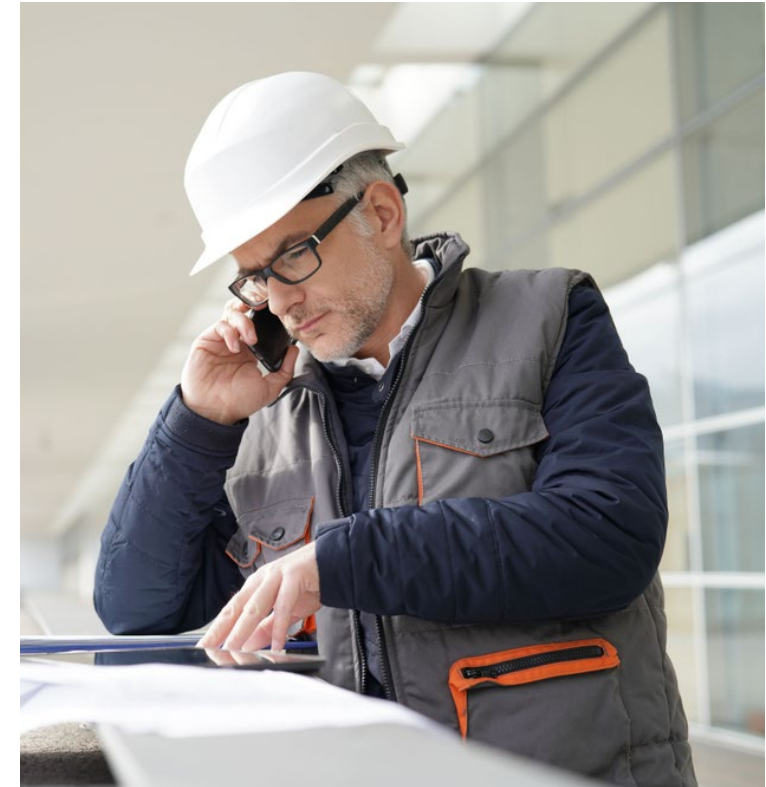
- Size
- Industry
- Management
- Comparability Data
- Medium Business



Scott Stone at 45

In order to help us build your Reasonable Compensation profile, tell us a little more about yourself and your business:

Industry	Specialty trade contractors
Occupation	CEO
State	Illinois
Metro area	Chicago
Number of employees	35
Adjusted Gross Profit	3.5 Million
Business performance versus peers	Above average
Owner experience versus peers	High
Hours worked per week on average	55



Scott Stone at 45

POTOMAC
Tax & Valuation

Page 1 of 4

Report for Scott Stone of Stone Concrete, Inc.

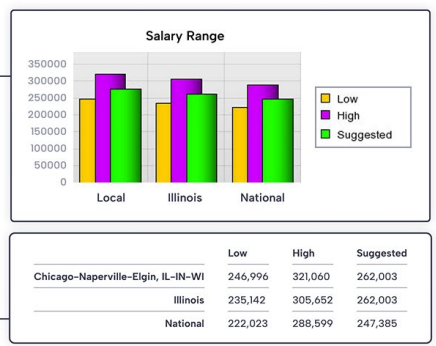
Your estimated annual Reasonable Compensation: **\$275,211**

Thank you for entrusting Paul Hamann of Potomac Tax and Valuation, PC with your Reasonable Compensation analysis. This report provides a reasonable estimate of the value of services rendered to your company based on the duties and responsibilities that you perform annually. The valuation of most businesses requires the owner(s) and key managers to have their compensation Normalized. Reasonable Compensation is defined as "The hypothetical replacement cost of an owner or key manager of a business."

Your suggested salary range: \$222,023 to \$321,060 with a suggested salary of \$275,211 was determined to be Reasonable Compensation based on your role in the company, industry, size of the business, time devoted to the business, your experience and location. Any wage selected within the suggested range or expanded geographical area(s) is acceptable and within a 90% confidence interval.

Reasonable Compensation Figure
Quickly view the calculated reasonable compensation figure with supporting details.

Reasonable Compensation Calculation
Details the salary range for the owner's industry and location and provides a suggested reasonable compensation figure.



POTOMAC
Tax & Valuation

Page 2 of 4

Report for Scott Stone of Stone Concrete, Inc.

Calculated for Scott Stone	Occupation Chief Executives
Company Stone Concrete, Inc.	Number of Employees (FTE) 25-75
Interview completed 2022-04-11 22:49:14	Adjusted Gross Profit 1m-5m
Report calendar year 2022	Business Performance vs. Peers Above Average
NAICS industry 238000 - Specialty Trade Contractors	Owner Experience/Proficiency Level High
MSA Location Chicago - Naperville - Elgin, IL- IN - WI	Time dedicated to the business Workaholic (65+ hrs/week)
State Illinois	

Business Summary
Details the inputs provided to reach the suggested Reasonable Compensation figure.



In order to help us build your Reasonable Compensation profile, tell us a little more about yourself and your business:

Industry	Specialty trade contractors
Occupation	CEO
State	Illinois
Metro area	Chicago
Number of employees	35
Adjusted Gross Profit	3.5 Million
Business performance versus peers	Above average
Owner experience versus peers	High
Hours worked per week on average	55

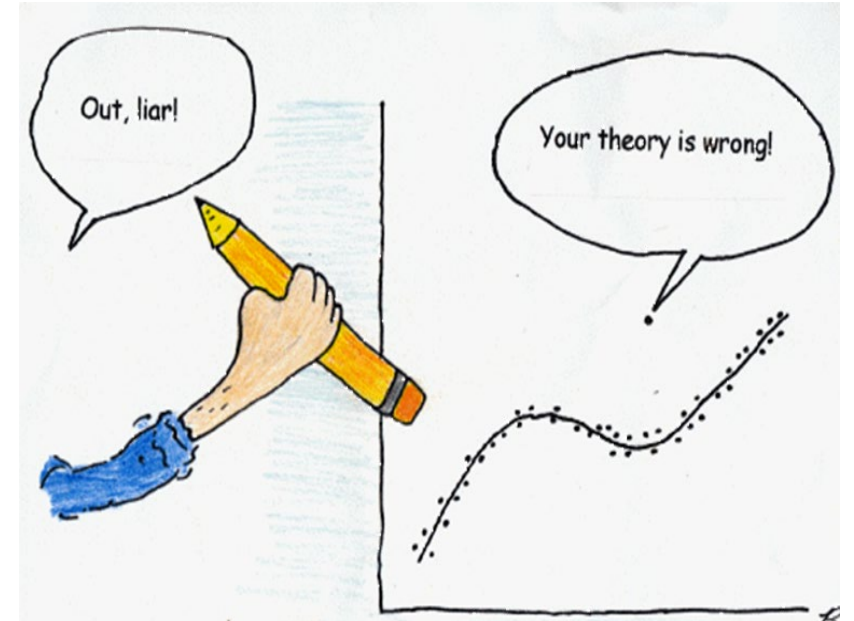
How – Income Approach

AKA Independent Investors Test



How – Income Approach

- No Comparable Wage Data
- ROI v. Reasonable Compensation
- Outliers
- 2nd Opinion/Test



Scott Stone at 55

In order to help us build your Reasonable Compensation profile, tell us a little more about yourself and your business:

Estimated FMV beginning of the year	6,000,000
Estimated increase in FMV by year end	1,750,000
Target return (independent investor rate)	20%



Scott Stone at 55


Page 1 of 5

Report for Scott Stone of Stone Technologies, Inc.

Your estimated annual Reasonable Compensation: \$550,000

Thank you for entrusting Sam Miller of Potomac Tax and Valuation, PC with your Reasonable Compensation analysis. This report provides a reasonable estimate of the value of services rendered to your C Corporation based on your responsibilities and the duties that you perform annually. Reasonable Compensation is defined by the IRS as "The value that would ordinarily be paid for like services by like enterprises under like circumstances."

The calculated salary of \$550,000 was determined to be Reasonable Compensation based on the increase in the Fair Market Value of your company over a one year time frame and a Return on Investment of 20.00% in conjunction with your efforts.

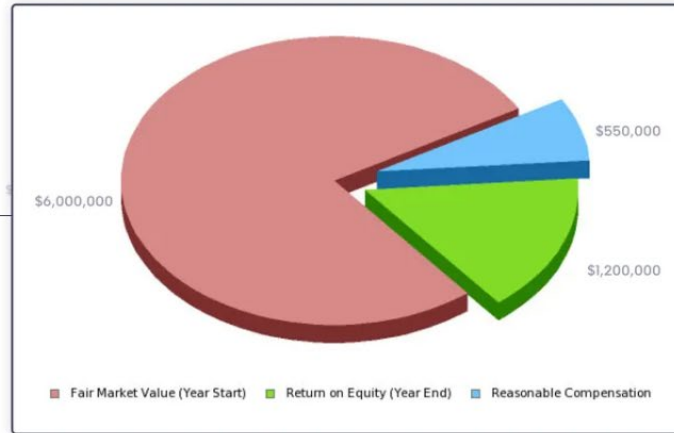
Potomac Tax and Valuation, PC recommends completing a Reasonable Compensation report annually.

Reasonable Compensation Figure
Quickly view the calculated reasonable compensation figure with supporting details.

Reasonable Compensation Calculation

Based on what a hypothetical investor would be satisfied with when looking at the financial performance of the business in conjunction with the compensation level of the owner.

In this approach, if investors obtain returns above what they should reasonably expect, an employee's salary is presumptively reasonable. This approach can only be used when you have Fair Market Value (FMV) for each year compensation is being evaluated.



In order to help us build your Reasonable Compensation profile, tell us a little more about yourself and your business:

Estimated FMV beginning of the year	6,000,000
Estimated increase in FMV by year end	1,750,000
Target return (independent investor rate)	20%



Custom Reports in Minutes


Choose between the three IRS approved approaches and tap into the largest source of credible wage data in the country to quickly create accurate, customized reasonable compensation reports for your clients.



Protection & Compliance

Take this quick, 2-minute quiz to assess your risk posture when it comes to reasonable compensation.

Page 1 of 7


POTOMAC
 Tax & Valuation

Report for Scott Stone of Stone Concrete, Inc.

Your estimated annual Reasonable Compensation: **\$68,788**

Thank you for entrusting Sam Miller of Potomac Tax and Valuation, PC with your Reasonable Compensation analysis. This report provides a reasonable estimate of the value of services rendered to your S Corporation based on your responsibilities and the duties that you perform annually. Reasonable Compensation is defined by the IRS as "The value that would ordinarily be paid for like services by like enterprises under like circumstances".


The calculated salary is determined by the number of hours the work is performed annually. You told us that you work 2080 hours per year. The duties and responsibilities that you currently perform.

Cook County, IL

Potomac Tax and Valuation, PC recommends completing a reasonable compensation report annually.

Your Time

Breakdown of how the owner spends their time in the business. This information is based on the interview completed.




Category	Percentage
My Business	60%
Management - Supervision	15%
Purchasing - Inventory - Shipping - Receiving	10%
Accounting - Finance - Bookkeeping	10%
Advertising - Sales - Marketing	5%

Reasonable Compensation Figure

Details the salary range for the owner's industry and location and provides a suggested reasonable compensation figure.

Your Compensation

How the compensation number is affected by each task the owner performs.



Category	Percentage
My Business	67%
Management - Supervision	18%
Purchasing - Inventory - Shipping - Receiving	6%
Accounting - Finance - Bookkeeping	5%
Advertising - Sales - Marketing	4%

Reasonable Compensation Figure

Details the salary range for the owner's industry and location and provides a suggested reasonable compensation figure.



Resources to Educate Clients


Solidify yourself as a Trusted Advisor to your clients by using the resources we provide to educate them on the compliance and tax planning issues related to reasonable compensation.



Increase Firm Revenue

Reasonable Compensation acts as the gateway to advisory services in your firm. Most of our clients charge for Reasonable Compensation reports, either ad-hoc or as part of a package offering.

Page 1 of 4


Report for Scott Stone of Stone Concrete, Inc.

Your estimated annual Reasonable Compensation: \$275,211

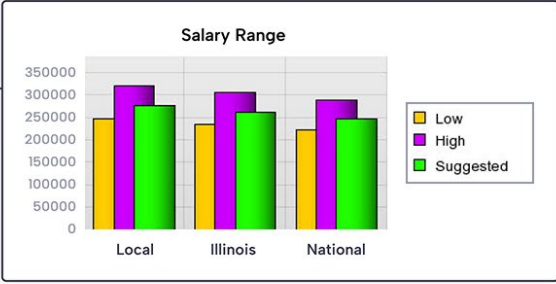
Thank you for entrusting Paul Hamann of Potomac Tax and Valuation, PC with your Reasonable Compensation analysis. This report provides a reasonable estimate of the value of services rendered to your company based on the duties and responsibilities that you perform annually. The valuation of most businesses requires the owner(s) and key managers to have their compensation *Normalized*. Reasonable Compensation is defined as "The hypothetical replacement cost of an owner or key manager of a business."

Your suggested salary range: \$222,023 to \$321,060 with a suggested salary of \$275,211 was determined to be Reasonable Compensation based on your role in the company, industry, size of the business, time devoted to the business, your experience and location. Any wage selected within the suggested range or expanded geographical area(s) is acceptable and within a 90% confidence interval.

Reasonable Compensation Calculation

Details the salary range for the owner's industry and location and provides a suggested reasonable compensation figure.

Salary Range



	Low	High	Suggested
Chicago-Naperville-Elgin, IL-IN-WI	246,996	321,060	262,003
Illinois	235,142	305,652	262,003
National	222,023	288,599	247,385

Reasonable Compensation Figure
Quickly view the calculated reasonable compensation figure with supporting details.

Client: **Scott Stone**
Company: Stone Concrete, Inc.

Step 01 of 05
Time & Location
Complete!

Step 02 of 05
Standard Tasks
Complete!

Step 03 of 05
Business Tasks
Complete!

Step 04 of 05
Tasking & Proficiency
Complete!

Step 05 of 05
Review

Step 01 of 05

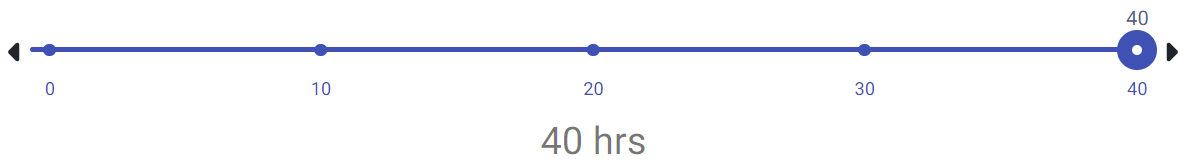
My Time & Location

My Working Hours

We need to know on average, how many hours do you work each week?

Be sure to set your hours! No hours = No compensation!
The Bureau of Labor Statistics defines 'year-round, full-time' employment as 2,080 hours per year (40 hours per week). If you work 'year-round, full-time' set your hours to 40+.

Drag the slider below or enter the hours manually to set your hours worked per week.



My Location

If you work in more than one state, select the one where your office is located or that you consider to be the predominant source of your income.

Search Address

Select State: Illinois
Select County: Cook County

Polling Question #8

Would you be interested in a personalized, 30-minute demo of RCReports?

A. Yes, that'd be great!

B. No, thanks

Want to Learn More?



Book a 30 Min Demo

Thank You



Paul S. Hamann

Founder RCReports



Eric L. Green

Founder of TRN

Want to Learn More?



Book a 30 Min Demo