TRANSCRIPT

On Your Terms

Episode #: 177
Can You Really Save Money on Your Taxes?
Guest Interview with CPA, Keila

Sam Vander Wielen:
Hey there and welcome back to On Your Terms. I'm your host, Sam Vander Wielen, an attorney turned entrepreneur who helps you legally protect your online business.

So, we're nearing the end of 2023, which I can't believe, and as you know, it's a really good time for reflection in your business, intention setting, and talking about taxes, unfortunately. So, while I know that taxes are not the most exciting topic of all time, I also know it's super important. And doing a couple of things now to make sure that you're prepared will save you a load of time and trouble next year, and hopefully save you a little bit of money on your taxes.

So, today we're revisiting a greatest hit from last year where you'll get the lowdown on everything you need to know about taxes, quarterly tax payments, saving money, whether you really can save on your taxes, all that kind of stuff. And I thought no one better to come in and help you with this than tax expert and CPA Keila of Little Fish Accounting. I hope you enjoy the episode.

Hey, Keila. Welcome to On Your Terms.

Keila Hill-Trawick:
Thank you so much for having me. I'm excited to be here.

Sam Vander Wielen:
I'm so excited for you to be here. I know this is a very highly requested episode and people are going to be so excited to chat with you. I had you come and chat to my Ultimate Bundle members in our little business building retreat back in October, and they absolutely loved it, so thank you so much for doing that.

Keila Hill-Trawick:
No, that was amazing. I love being able to share things that I think people have heard or have heard something about but don't exactly understand what it means, so it was nice to see all of the light bulbs flashing around the room when I was there.

Sam Vander Wielen:
Exactly. I mean, you and I have such, I feel like, similar businesses in that respect where I think we are like light bulbs turner on our people. And I was wondering - I have my own thoughts but I'm so curious - why do you think people are so confused and rightfully freaked out by taxes, even more so when it comes to their business, maybe, than personal stuff?

Keila Hill-Trawick:
I think, one, we don't really talk about the life cycle of taxes enough. People think about a tax return being due on a specific day and that's the only time that they have to think about it. And so, first, starting from a place of this is how taxes work, this is how what you pay gets reflected on your tax return at the end of the year. But I think the other part is there is so much information and misinformation about either saving taxes or not paying taxes so that most people think that there are more loopholes available to them than there actually are to get them out of paying taxes, as opposed to the conversation being around how can you prepare based on where your business is, how much money you're making, what's going on to actually make those tax payments while taking advantage of all the deductions you can.

Sam Vander Wielen:
Exactly. Yeah. I think you're totally right that we do overcomplicate it that it almost seems like this super elusive, almost like a game that you can win but you've got to find the right pieces. It's like when we used to have Game Boy when I was little and you're always looking for the little thing that was hidden somewhere.

Keila Hill-Trawick:
It's basically Tetris.

Sam Vander Wielen:
It's Tetris, yeah. I think that's what people think it is. But for our kinds of businesses, for online businesses, online coaches, the kinds of people that I help, what would you say to them how do online business taxes work? How do taxes work for our kinds of businesses?

Keila Hill-Trawick:
Yeah. So, I would say the first thing to remember is that you are paying taxes through the year and before. And so, everything that you're paying taxes for in February, March, April, depending on when your return is due or when you're ready, is based on January 1 through 12/31 of the year before. The reason that that's important is because I think people think that there's more flexibility or more work that they can do after the fact that isn't available. As much as we can, we want to get all the things done throughout the year.

And so, all year long, you're earning money - hopefully - you're spending expenses and you're earning a profit. And every IRS quarter, you are making an estimated payment that essentially says I think I'm going to owe about this much when my tax return comes. And so, you're making those payments throughout the year. If you happen to be a person that also has a W-2 job, every time you get paid, they're withholding taxes on your behalf, sending them to the IRS and the state for you, again, as an estimate to say based on what she is making here, I think that she's going to owe about this much in taxes.

And if you think of all through the year those amounts being estimates, your tax return is essentially settling up. So, what you're saying is, "Okay, IRS. Here is my paperwork. It turns out that I actually made this much at my W-2 job. I totalled this much at my business. This is all the money that I brought in, my deductions. Here, this is my taxable income," after you get to all these places. And then, there's some magic that happens with tax tables and all that, and your tax preparer through the IRS and the state says, "Okay, cool. This is how much you owe in taxes."

In this example, let's say it's about $10,000. The next line says, "Oh, but I paid you some of that already. Because, remember, last year while I was getting my check, you took $5,000 out in taxes there, and then I made estimated payments to you as well." And the difference determines whether you get a refund or not. So, if we use that $10,000 as an example, if in total what was withheld and what you paid in estimated taxes was $12,000, You get a $2,000 refund. If you underpaid, the amount that you owe is the difference.

That's why I tell people, it's really important that you think about when you're looking for a tax preparer the fact that, to some extent, we cannot actually save you taxes. You owe what you owe. And the goal is that you are prepared and that you are paying enough. We obviously can see deductions that you might not have been aware of or other amounts that can kind of change your tax plan. But for most people who are falling into this space who are not incredibly high net worth, you're saving taxes by spending money. And so, we just want to make sure that you're spending that appropriately and, again, that you are prepared for the fact that there will be a tax burden. You're just trying to pay as much as you can in advance.

Sam Vander Wielen:
Yeah, okay. So, yeah, I always think of the quarterlies as almost like a savings plan with your taxes, you're just paying it every quarter so that you're not getting hit with this giant bill come, for some people, April 15th, for me being an S-Corp, March 15th, being like, "Oh, my gosh. We owe how much." But instead it's like you've been making little deposits every quarter along the way. And then, technically speaking, come the next year, we should not owe or owe very little or, at the very least, just have a good idea of what we're still going to owe for tax liability. So, that's the federal part. We've talked through federal, but then we also have to talk everybody through then what happens in their state, so they also have state taxes. How does that work for us?

Keila Hill-Trawick:
Yeah, so it's very similar. I will say for the most part, most state things are just a reflection of what happened federally. So, your federal return is finished, all of that information kind of gets copied and pasted, for lack of a better term, into your state return. And then, any state related

deductions that you have access to, I'm thinking about things like 529 plans, maybe some energy efficiencies, maybe some dependent credits that you don't get from the federal, you'll get on the state. And it's the same idea, all the money that you've made, all the money that you have spent that they've already accounted for.

And then, the state tax rate is a little bit less complicated than federal because it's usually a flat rate. So, a state tax rate might be 6 percent for individuals, as opposed to a federal tax rate is, like, well, it's 12 percent if you make between this much and this much. They typically don't have those brackets.

Sam Vander Wielen:
Okay. All right. So, we've knocked out then that when it comes to online business in terms of how do taxes work, we're looking at paying federal taxes, then we're looking at carrying that over to also paying whatever our state requires, unless you're lucky enough, I guess, to live in one of the states that has no income tax, I guess, but we do not, neither of us do not.

Keila Hill-Trawick:
We do not.

Sam Vander Wielen:
Neither of us get to do that, but that's all right. I think it would be helpful for you to talk a little bit about the expenses and the cost of running a business, because I know that so many people ask me when they're in the early stages of kind of still setting up and forming their businesses, can they capture expenses before they've even registered?

Keila Hill-Trawick:
Yeah. So, let's talk first about the rule of deductibility or the rules from the IRS. And the rules for you to be able to deduct an expense are that they are (1) ordinary and (2) necessary. So, ordinary means that these are common in your industry. Your peers are incurring the same types of expenses. People who do what you do are spending on the same types of things. And then, necessary really doesn't mean necessary the way that we

typically define it, it just means that it's helpful for your business. So, I always laugh when one of your parents would be like, "Do you want that or do you need that?" It's not that. It doesn't have to be indispensable to your business. It just needs to be helpful for you to be able to perform the work that you do. And so, once you have established that, it meets those two criteria.

The second thing about startup expenses is to remember that we capture everything that has happened in a year. So, I'm less concerned if you started spending expenses in January, February, March, and you didn't officially get your LLC or register your business until April or May. We're going to take the whole year and I'm unconcerned about those three months before we're just going to capture those any other deductible expenses.

If you have a year or several years where you are spending money, but the business isn't really ready to kind of be open to the world yet, there are different rules about how you'll capture that, how you have to kind of break those out across future years.

But I would venture that most people, one, are already up and selling. Their business just isn't official with the state yet. Those are not startup. If you are ready to make money from the business and also incurring expenses, we're going to treat you tax-wise just like if your business was registered. We're putting all of that on the same form to make sure that you have the ability to deduct those and that we're capturing any and all revenue that you earned in the period.

Sam Vander Wielen:
Okay. That's super helpful. And do you tend to find, like, are there any expenses in our industry that you consistently see people reaching out to you being like, "Hey, Keila. I got this expense." And then, you're like, "That's not a qualified expense."

Keila Hill-Trawick:
Yes. First of all, I call it LLC Twitter and Instagram. We'll have y'all thinking that you can deduct whatever you want as long as business kind of

touches it. Like, "Did you say something about your business? Deduct this whole meal." That's not true.

Sam Vander Wielen:
Yeah. That rumor is so annoying where people will be out to dinner and they'll be like, "Oh, we talked about our business." Or my favorite, too, is on Instagram, you'll see people be like, "I wanted to write captions for my business so I flew to Paris for the weekend. Like, I'm so glad it's a business expense." I'm like, "That is not a business expense."

Keila Hill-Trawick:
To get inspired. It is not. It is not. This inspiration of like, Are you a French teacher? Because then Paris might count. But are you a social media manager that just wants to look out over the Eiffel Tower? Not so much. So, yes, definitely meals and travel expenses that people assume are deductible because they mention business or I think the idea that you work while you are on a trip doesn't make it deductible. The idea is that the trip's intention was for work, that you went because there was a conference or you went to meet up with people or you're a designer and you went to a show or something like that. All of that is fine. But the idea that I went somewhere else on vacation and happened to work while I was there does not make it a deductible expense.

The other thing that comes up a lot, especially in this age of branding and rebranding and video and showing up in these places, is clothes. A lot of people think that I had to show up and look nice for my photoshoot or for these videos that I was going to put up, so I should be able to deduct the clothes. And the IRS is typically like, "Nuh-uh. It's not a uniform if it doesn't have your business's name on it."

What I will sometimes do is if these are outfits or clothes that are technically not deductible but are only incurred because of - so I'm thinking about you're going to a major gala for your business and you have to buy a ball gown of some kind, yeah, the IRS is going to say no - well, they would typically say no. I think we could make the case for that being partially deductible. Yes, you could wear this later, but also the only reason I went to rent the runway is because I had to get a dress for this night and I'm sending it back. That would be a different expense than I bought five new outfits because I'm going to show up on video more this year, the IRS is going to say no.

Sam Vander Wielen:
Yeah. Well, this is why you should all steal my secret, which is just showing up on camera the way that you want to look because you don't even have to worry about it.

Keila Hill-Trawick:
Right. Wear your regular clothes and set appropriate expectations. That's what I do too.

Sam Vander Wielen:
Just be a human and then no one cares. And then, you can rewear that hoodie wherever you want to go. That's my method.

Keila Hill-Trawick:
And you were already going to buy it. You were already going to wear that hoodie. It is not because you have a business.

Sam Vander Wielen:
We can slap a Sam Vander Wielen logo on it.

Keila Hill-Trawick:
Exactly. Stick something, it's hilarious.

Sam Vander Wielen:
This was really funny, this hilarious fail in this department. We ordered the team these sweatshirts that was for team gifts and whatever, and they had cute logo, our business logo on it. Well, the lady who we ordered from neglected to mention that they were crop top sweatshirts. But they were not just cropped up. They barely covered the front. And it was so funny.

Keila Hill-Trawick:
They're children's sweatshirt.

Sam Vander Wielen:
They literally are for children between the ages of two to three. We got them and I literally held it up, I was like. "Where's the rest of it? What is this supposed to cover?"

Keila Hill-Trawick:
"I think you forgot to put some fabric on here, ma'am."

Sam Vander Wielen:
It was so funny. So now, we have this giant box of these hoodies with my logo on it that are for very small children. So, if anyone has a child who would be interested in wearing my hoodie, you just give me a shoutout, I will send you one.

Keila Hill-Trawick:
Listen, and it's still deductible. They did not work. Nobody can wear them. But you still get to deduct it on your taxes.

Sam Vander Wielen:
I know. And I'm always very nice about this stuff. And I emailed the lady, I was like, "I'm not asking for a refund or anything. I'm just letting you know, in the future, you should probably let people know they're about four inches long. Most adults don't want them."

Keila Hill-Trawick:
"Just let them know they are tube top hoodies. And not actual hoodies that you can wear outside."

Sam Vander Wielen:
It was hilarious. But, yeah, that was a business expense gone wrong.

Keila Hill-Trawick:
We could get a whole series on that, business expenses gone wrong.

Sam Vander Wielen:
Yeah, seriously. We could have stories for days. Well, anywho. Okay. I think that's really, really helpful. I mean, so you helped us walk through

things that people think are expenses that aren't. Are there some things that maybe people think aren't that are?

Keila Hill-Trawick:
Yeah. A couple that come up a lot are, one, books, magazines, periodicals. So, the reading material that you invest in, in order to get better at your business. If I move, you can see that I have a bunch of business books behind me, all of those are business development expenses to some extent of me trying to make Little Fish better. And so, one, definitely books, periodicals, subscriptions that you're paying for in order to make you better at what you do.

The other one actually is a cellphone, that a lot of people forget, I think, because they pay for it out of their personal account, and so they forget that it's deductible. This is another one that I would say is probably partially deductible. So, most of us are doing a ton of things from our phones. We are on social media, we are emailing clients, some people even text their clients, you may be creating content on your phone. And so, all of that really makes it business work versus personal work on your phone. And what I typically tell people is to think about an estimated percentage of how much you use your phone for personal versus business, and then deduct that portion of what you pay for both the bill and the phone.

Sam Vander Wielen:
Yeah, that sounds like a really good idea. Sadly, I feel like my percentage wouldn't be so high. I remember telling my accountant it's, like, 90 percent because, sadly, I use it so much for work that I put it down, I don't want to look at it. I actually joked with Ryan yesterday that I want to go out and get a flip phone just for my personal number so that it has nothing on it and then just have my phone and leave it in my office.

Keila Hill-Trawick:
I keep thinking that. When I open my phone, I'm like, work is waiting for me, so nevermind. I don't want to go.

Sam Vander Wielen:

It's all it is. And nowadays it's also our camera. I'm using it for all videos, all this kind of stuff for Slack, for Vox, for all the things. So, yeah, you guys probably are using it way more than you think, so that should be helpful. I guess technically, well, if you have an iPhone, you could look at the app usage thing where it breaks down for you what percentage and what time you're using. Because I actually have mine categorized, so it'll say like work apps and all of that kind of stuff. That might be an interesting way to look at it.

Keila Hill-Trawick:
Yeah. That's a good way. And, typically I tell people to start at, at least 50 percent and then go up or down from there based on how much you're using it. But that would be really good backup in the event that the IRS asks about it.

Sam Vander Wielen:
Yeah. They challenge you on it. Okay. That's good to know. So, are there tax implications that somebody should consider if they're about to register their business and they're deciding between registering as a sole proprietor and an LLC?

Keila Hill-Trawick:
No. I'm glad you asked that question.

Sam Vander Wielen:
Thank you for backing me up on it. I just needed my Keila backup. Thank you.

Keila Hill-Trawick:
Exactly. So, an LLC is considered a disregarded entity by the IRS and by most states, and what that means is that they do not care that you're an LLC. From a legal perspective, obviously, there are a ton of benefits if you're doing it right and you're keeping your stuff separate, and all of those things, not just creating an LLC - but I'm not a lawyer.

In tax land, the sole proprietor and the one person LLC are taxed exactly the same. As long as you haven't elected S-Corp treatment, it's going to go on a Schedule C with all of your revenue and expenses. And so, keep in mind that anything tax-wise that you want to do with the business, whether that's hiring employees, paying contractors, opening a business account, all of those things can happen without an LLC, as long as the business is registered, has an EIN, and is set up to give those institutions the information that they need.

Sam Vander Wielen:
Yeah, exactly. I mean, the legal perspective is different, and we talk about that a lot here. But then, I think for some reason on my end, people, they'll hear me talk about the legal benefits of the LLC, and then I'll always say, like, "I know it sounds really funny because I just told you a sole prop has no legal protection, but you actually get treated, in the eyes of the IRS, as a sole prop for tax purposes."

But there's two categories, like Kiela said, there's the tax category and the legal category. And for you worrying about getting sued, I'm always talking about the legal category, so it's totally, totally different. But I think people do think there's some weird hidden LLC tax and so they're always like, "Oh, I haven't made enough money yet to become an LLC" or I'm not profitable yet." I'm like, "That has nothing to do with it."

Keila Hill-Trawick:
They're not relevant. As you have talked to everyone about, this is really about risk mitigation and not about taxes. I'll say two things about that too. One, setting your business up as an LLC is not incorporating it. So, I think that people will often say, "Well, it wasn't a real business before. I hadn't incorporated it yet. I hadn't made my LLC." And so, when we go back to those expenses that happened before, again, you have always been a business as long as you have been open for business, even if you haven't filled out that paperwork.

The other thing that I'll say about that is that the LLC gets touted for a lot of reasons because it just is popular right now for people to really call out. You have to decide what type of risk you're willing to do, what types of other steps that you need to take to make sure that the LLC is even enforceable. Like, this idea that I will just checkbox, I have an LLC and now I'm good going forward isn't true.

Sam Vander Wielen:
Right. Exactly. That's why I always say to people, it's not a checkbox. And that your state might require that you have an operating agreement or your business money is still not protected, so that's why I talk about business insurance. It's like, great, you're not personally on the hook, but can your business sustain a lawsuit? It's huge. So, there are many other factors. And it's also why I teach people how to act like an LLC, too, because a lot of people don't know about that, which you talk often about keeping expenses separate.

So, one of the ways that I remember as an attorney, we used to go after people and try to pierce the corporate veil when people had LLCs was that they were treating business money like it was their personal money. And so, they were either literally commingling funds or using business revenue to do some of the things we were just joking about, like going to Paris or buying a Chanel handbag or whatever, and then we were like, "Look, it's not really an LLC. It's a personal hobby. So, therefore, we can go after them personally."

Keila Hill-Trawick:
Yeah. And that's a really good point when we talk about commingling funds, because often when I'm asked what is the best way to save taxes, it doesn't always register, but the best way is good bookkeeping. And so, the better you can see exactly what is going in and out of the business, the better you are keeping them separate so that you're not trying to look in your personal account for stuff that you think you paid for, for the business, or doing this mark out of these four things that are on my business card are actually not business. The better that you can do that, the more that you can plan for tax savings, the better that you can build strategy for your business because your numbers are accurate, you can trust them.

And so, I think bookkeeping can get kind of a throwaway idea of, "Oh, I would just pay somebody cheap and they would just put numbers into the right categories." But it really sets the foundation for everything that you're doing in your business. And so, if that is not right, all of the decisions that you will make as a result are going to be wrong too.

Sam Vander Wielen:
Yeah, that's true. And so, I guess along those lines then, I was wondering, when should someone hire a bookkeeper? And at the same time, what are some of your favorite tools for keeping track of those expenses and revenue? Because maybe somebody's doing it themselves right now and they want to get it set up, but then they're going to hire a bookkeeper to help them keep track of everything.

Keila Hill-Trawick:
Yeah. So, I always highly recommend that you understand your books before you give them to anybody else. One, I've seen too many horror stories of people who are not in their own accounts, didn't really know what was going on. And then, we come in and we're like, "What is this? And what does this mean? And why is this this way?" And they're like, "I don't know. My account did that." You are the CEO of your business, you know more than anybody else, and so your ability to read, interpret, and be able to act on financial statements is really going to be a superpower in how the business grows and is able to do new things.

The other thing that I would say is get into an accounting system as soon as possible. I know it can be tempting to be like, "I don't even have that much going on. I'll just use this spreadsheet," but it is super manual. And when you first start your business - not even when you first start, we both know there's just several layers of you wearing too many hats at your business. And the idea that you would have to then remember to put in income and expenses that have come in that week as opposed to your bank account being attached to a system that will pull that stuff in automatically is a recipe for you losing out on deductions because you don't remember. Forgetting to put some income in because somebody paid you in cash and you only deposited some of it because you used the other part on dinner, all of those things get really hard to track when you're doing it yourself.

And then, I would say, finally, when you're thinking about what to outsource, we have a guide for that, but you really want to think about what your priorities are. So, we always say in the order of, first, tracking. So, the first accounting professional that you want to hire to help you with should be doing some bookkeeping. They are categorizing transactions, reconciling your accounts, making sure that there are no duplicates and no missing items. They are making sure that your books are accurate.

Then, compliance. Usually that happens at the same time where you're hiring a bookkeeper and a tax person. We happen to do both in our services, but not all accountants do. So, you just want to make sure you're picking the thing that makes the most sense.

Then, we talk about strategy. So, having somebody that's really analyzing your financials, talking to you, and being proactive about what's going to be next for you. And then, finally, outsourcing. When you get to the point where you're like, "I don't want to touch this anymore. Somebody else can just do all of this."

But at the very beginning, you're tracking and your taxes are going to be the most important parts. And if you feel like you can track, because I know that there are some online business owners who, say, teach cohorts, and so they're like, "I get a bunch of money in and I have expenses, and that only lasts for three months, and then I have a break. I don't need to pay somebody to constantly do this." Just make sure that you have the right education to be able to take care of it, because bookkeeping is very easy when it's going right, and it is very difficult to correct when you make mistakes.

Sam Vander Wielen:
Yeah. Isn't that the truth? I was like, "Get this away from me as fast as humanly possible. I will outsource this." I'm also very much of the mindset these days where, like you said, I wanted to kind of get my hands around it because I hate handing stuff off to people for I have really given it a crack. But I wanted to start acting like the business I was becoming. And even though my business at the time didn't have so many payments flying in

that I technically couldn't have handled it myself, I was like, "Yeah. But I'm building a business that's going to have so much of this coming in, coming out that I'm not going to be able to handle it." And like you said, we have so many hats to wear, but I don't think we have to put them all on. It's like, let's get rid of it.

Keila Hill-Trawick:
No, I agree with that. And I think the other side of this is the understanding that you don't want to have to hire out of desperation. You want to hire somebody that you can trust at the beginning when you're making a little bit and you're just still growing because that person knows your business well enough.

We say at Little Fish a lot, we grow with you. Because then by the time you're in virtual CFO and you're handing it all off, I know everything about the business and how we got to this place and how we're looking at this. You really want to establish that relationship early on because, you're right, people tend to think I don't need this right now so I'm not going to worry about it. And what I would encourage everyone to do is say I know I am going to have to worry about it and I already want to be in a position where, when I'm ready to hand that off, somebody that I trust is there to catch me.

One example that I'll give is that we have had on a couple of occasions where somebody is trying to get a brick and mortar space or buy a house or get a loan, and they need a letter from their CPA. Well, if I'm not your CPA because you're a person that just reached out for service, you don't have somebody already in your corner to be able to do that for you. And so, the relationships that you can build with your service providers, especially your attorneys, your accountants, your advisors on the frontend really help you to be more hands off as the business grows because you can trust that they're taking care of you.

Sam Vander Wielen:
Yeah. It's very true. And now that I've bought two houses and owning a business, I can tell you that having such clean, organized books and having everything reconciled all the time, having P&L statements every month to

hand over was just like, "Okay, cool. This is good. Thanks. Just keep updating us," because, you know, it took 90 days or whatever to settle. So, I would send them the next month, the next month until we closed, and that was it. But there was no questions. Nobody asked for anything.

And I think there's a lot of fear. Actually, someone had asked me to do like a podcast episode about buying a house when you own your own business. And I was thinking about that, it was like, well, most of it is just what we're talking about, it's keeping your head down, doing good work, and building the business, but having everything really organized and clean on the backend so that you have all this proof and you look super legitimate and professional like you look like a real business.

Keila Hill-Trawick:
Yeah. And it takes away a lot of the anxiety and fear. Finances just have so many feelings surrounding them, and I think a lot of that is from being unorganized. Like, when taxes can feel like you got all the documents there in the folder, I can just send them over, that is a completely different experience than "What did you ask for? I think I saw that in an email. Or they delivered it to my house and it was on the kitchen counter, but now I can't find it." That's where a lot of the stress comes in. It's not about math. It's not about being great with numbers. It's about this understanding that you are not rushing at the end.

That also comes with bookkeeping. Even if you're doing your own bookkeeping or you're ready to hire somebody, your first step is a gut check, like does this even look right? If it says that you have negative $4,000 in your bank account, that is a flag. This is probably not right. When you're looking at your bookkeeping every month and checking it to say, "Does this even make sense to me? Does my P&L make sense? When I look at it, does it seem like I earned that much last year? Let me dig in and be able to see what makes up that number. This number for contractors seems really high, I don't think that I spent that much."

You also want to make sure that you're engaging a professional that will answer your questions. You don't deserve to be belittled or be treated as if you're wasting somebody's time. And I think we've talked about in the law and accounting world, because a lot of it from a corporate standpoint was based on billable hours and people being kind of worth your time, I think that gets passed a lot to small business owners where they will try to engage somebody and somebody is being condescending or making them feel stupid. Get somebody at the beginning of your journey where you can ask all of the questions because, eventually, you will get to a place where you don't have as many questions, but you at least trust that somebody is looking out for you.

Sam Vander Wielen:
Yeah, totally. I think that's really, really good advice. You know, something that came up after I did this episode on how to pay yourself as an owner, which was more from the legal perspective because I think people think they're doing something illegal when they write themselves a check, they're like, "Is this wrong?" So, I'll link below for the episode that I did about how to legally pay yourself as a business owner.

But one of the questions that I get a lot, which I'm always just like, "Oh, I can't tell you this," is how much that someone should pay themselves. People always get stuck on how do they determine what's an appropriate amount to pay themselves as a business owner.

Keila Hill-Trawick:
Yeah. So, let's talk about two different roles. So, I'm going to get to paying yourself as an employee and payroll if you have an S-Cor, but let's just start with you being a sole proprietor or a single member LLC that is taking draws.

Because you are not paying yourself a salary. What we think of as paying yourself is payroll. You're running payroll. Payroll taxes are coming out. Benefits are getting paid to you, if you're entitled to those, all of those. But if you're taking these draws, the first thing that I say is budget for what you want to be able to pay yourself consistently. So, even though you are not on payroll yet, a lot of people are asking from a place of how do I replace my W-2 salary? How much should I be paying myself so that I can afford to live all of that?

Well, we got to start with something. So, maybe you are making $4,000 a month. Maybe that's where your draws start. I'm going to try to take $4,000 a month and see how it affects cash flow. Cash flow is the number one reason that small businesses fail. And so, you really want to make sure that you have an understanding, when I take this 4K out to pay myself, is there enough to cover all of the other expenses that the business is going to go into? And that may need to be adjusted. It can be adjusted either way. You may go in and say, "Oh. Okay. My business is at a place where I could pay myself $3,000," not 4,000 and we will try to go up. The other side is, "Actually, it turns out I have more money than I thought I did, I could pay myself 5,000."

So, start at a place. There is no penalty or restriction against moving how you give yourself money because you're not on payroll. So, take advantage of that flexibility to figure out what number looks right to you.

I would say then, be aware of what your job is, it is really important. Especially as you think about hiring a team or potentially having people help you, it's really important that you start from a place of "Well, how much do I got to pay them?" Because if you are paying yourself the same amount that you're paying, say, an entry level marketing coordinator, I want to figure out how to make some more money so that you as the CEO can be really paying yourself what you're worth.

And then, I think finally, something to think about is where your money is coming from in order to determine your salary. Especially for those business owners who are maybe selling products or group coaching or something that has more bodies in it alongside maybe a one-on-one or done for you service, you want to be able to see how much of that is recurring, how much of that is expected, because that will also give you a sense of if I can make X amount every month on this recurring revenue, I know I can give myself this much, even if I'm only launching this group program or these planners or these other products twice a year. Those are basically just bonuses to the business, but I'm not reliant on them to cover myself and other operating expenses.

Sam Vander Wielen:

Yeah, totally. Okay. And what you pay yourself, as I mentioned in that episode, is not a business expense. I think it's just something people don't think about when looking at that amount. I remember I used to be like, "Okay. I could pay myself $3,000, but what I'm going to do instead is pay myself $2,000 because I also need to leave money left over for tax liability and paying my taxes and then stockpiling for future expenses and to be able to build up some capital," which really gave me the runway. I think that maybe people don't think of it enough just because you can pay yourself, especially early on, doesn't mean you have to necessarily, unless obviously we need to do what we need to do to live. But it was also a reason why I kept working in the beginning.

And so, sometimes I think that this question comes from a place of this expectation that the business is supposed to generate enough immediately to cover their living expenses, and they're like, "Well, how am I supposed to live off of that?" I'm like, "Well, I just kept working." I still worked as an attorney because the business couldn't make that much money. And it wasn't until it could that I let it go.

Keila Hill-Trawick:
Yeah. And I talk a lot about that, too, even on my journey. Like when I started Little Fish, I was working for the government, I was making six figures, and I was married. And so, I had a lot of benefits by the time I quit my job to do this fulltime. My husband had health insurance. Because I'm a wife, I don't have to pay for my own health insurance. That's a really expensive amount for a lot of individuals if you don't have that. Of course because I have a spouse, I also had a person who was also bringing in money. So, it wasn't like I need to cover this household by myself for the money that I'm bringing in.

And so, to your point, yeah, for my first year of business, I worked fulltime for the government. Because I was making over six figures, I also had disposable income that I could put to the side. This is a much different conversation if I'm making 40K a year or 50K a year, Little Fish would have had to generate a lot more for me to be able to live. And so, because I had disposable income that I could save, when I quit, first of all, I quit in the middle of tax season because I knew that I was going to get paid at least for the next two, three months, and then we would see what the business did, but I had savings. And so, whatever that combination needs to look like for you, I always say there is no W-2 shame. You need to do what you need to do. Entrepreneurship is not for everybody. Full time entrepreneurship is not for everybody. There's a variety of different ways that we can make lives that we love from work.

But to your point, that also needs to come with some realism about the fact that your business today can probably not pay your mortgage. And if it can't, how can you make enough money so that you're not feeling scrapped by the fact that you relied on your business to give that to you and it just couldn't.

Sam Vander Wielen:
Yeah, that feels like so much pressure on a little baby business. And so, when I hear people saying that I'm like, "Oh, my gosh. To generate enough to not only cover your expenses, but also pay yourself, and you just started, that's a lot, unless you're walking into something that you've got - I don't know - in the bag." But that's, to me, like going on a first date and pulling out your wedding planner and being like "Would you rather have vanilla or chocolate cake?"

Keila Hill-Trawick:
"Are you ready?"

Sam Vander Wielen:
It's just like, "Whoa, whoa, whoa. This is too much."

Keila Hill-Trawick:
"I just met you."

Sam Vander Wielen:
Yeah. "We got some mistakes to make, all kinds of stuff. It's too early."

Keila Hill-Trawick:
And I think also the thing to remember - and I've been talking about this a lot with clients too - is that your business will not always be profitable.

And that's not necessarily a bad thing. And so, your first year might be a foundational year where you're investing in things that you're not going to invest in every year. Maybe you needed a startup coach, or maybe you had to pay for all these businesses for somebody to make a website or help you with some contracting work that is not going to be every year, that probably is not the point to also say, in business, you need to be paying me.

So, to your point, not only do you have these operating expenses, you also kind of have these startup expenses that need to get out of the way so that potentially you can use some of that money to put back in your own pocket. But it's going to be very difficult to do all that at once while you're still trying to build the business from the ground.

Sam Vander Wielen:
Yeah, exactly. Yeah, I think you and I are on the same page about that. So, that kind of covers paying yourself for somebody, like you said, who's still the individual owner, like sole prop LLC, single member LLC position. But what about somebody who has an LLC, who has elected S-Corp taxation, like myself, who now, you know, we go through payroll, we use ADP, we do all the things, can you talk a little bit about that process in paying yourself as an S-Corp owner?

Keila Hill-Trawick:
Yeah. So, the one thing to know is that you are now an employer. So, I want the mindset to really adjust to not just you're paying yourself, where it's like, "Well, I don't take it as draws anymore. I just take it out of payroll." You need to set up a payroll system. You need to abide by the laws in your state about being an employer. And that's workers comp, that's unemployment, that is time off, all of the things that a regular employer would have to listen to, you got to listen to now too. So, remember that in addition to the salary that you're going to be paying yourself, you also have this additional administrative burden of just keeping up with being an employer in your state.

When you pay yourself, you are required to pay yourself a reasonable salary. As expected, the IRS is not real detailed about what that looks like, but I would say that you want to look at a couple of things. The first thing is, what is the market rate for your job title? Now, some of that's unrealistic, right? I am the CEO of my business. CEOs in real life make more than my business makes, so I cannot pay myself that. But you have a starting place for the positions that you're carrying, because it may be that, yeah, I'm the CEO, but because we don't have account manager, I'm spending, like, 30 percent of my time on that, 20 percent on administrative duties, and so that may break up what your salary looks like to amalgamate to this idea of how much you owe in total or you pay yourself in total.

I think the other thing to think about is, especially because most of us or many of us go into business for something that we already had expertise in, what is the common pay for that role, either from your experience what you used to get paid or from people who you would hire to do this job? And then, finally, really just looking at how much it costs to run your life. We want to make sure that what you're taking in salary is considered reasonable because you're not taking so little in salary and so much in draws that it doesn't make sense.

So, I've seen people who are, you know, paying themselves a salary of 40K a year, but then they're taking additional draws of a 100K. That's an easy audit flag for the IRS to say, "Clearly this 40K is not reasonable because apparently it costs you 140K a year to live." There might be some extenuating circumstances, maybe you're buying a house and needed to take some money out, there may be things that you can kind of back up.

But, one, you want to talk to a professional before you do that just to make sure that there aren't any obvious flags that would be raised to the IRS based on how you're paying yourself. And two, that it makes sense for what you do, that you can afford to continuously pay yourself that amount, and that it is reasonable within the context of what your job is really responsible for.

Sam Vander Wielen:
Yeah, that's super helpful. So, yeah, I'm glad you touched on that, that when you have an S-Corp and you still get a salary, or when you get a salary, you can still take owner's draws. I have, I take them from time to

time if shit gets really expensive or something happens and I'm like, "Oh. I need to cut." Or we're doing way better than we thought, I'll just take something.

The rumored balance I've always heard has been, when you're S-Corp, about 70 percent of your income should come from that paycheck and 30 percent could still come from the draws in order to not draw too much attention. Is that about right?

Keila Hill-Trawick:
Yeah, that feels about reasonable. Generally, it depends on the person and it depends on how much you take in salary. So, if you take 70-30 in $40,000, that's different than 70-30 in $300,000. What really feels reasonable? Overall, that seems like a decent breakdown. And like I said, I think the first step is to have that baseline - I'm working at about 70-30 - and then talk to somebody to make sure that there's nothing else that you're not paying attention to that could also hinder that.

Sam Vander Wielen:
Yeah, that's super helpful. And you always recommend that if they're going to go the S-Corp route, they always have their CPA help them to set this up and to make sure everything is filed properly, right?

Keila Hill-Trawick:
And I think it depends because not all CPAs do it. We won't establish a reasonable salary for you. We'll just point out guidelines that you should be aware of. We'll point out if we noticed any flags of like, "Hey. This salary seems really low. It might be something that you want to think about." But you at least want to get some advice on your situation.

Something else that I've seen come up that we talk about is, you know, I'm having a baby soon and I need to adjust my salary accordingly, or I'm getting married and this is what things might be different. You want to make sure before you make any of these major pivots that you have somebody that you can check in with and just say, "Hey, before I hit this button, am I not thinking of anything that I should be aware of?" even if they're not actually telling you the exact amount or what you should or have to do.

Sam Vander Wielen:
Yeah, totally. And when do you typically start talking to clients about you might want to start thinking about becoming an S-Corp for taxation purposes?

Keila Hill-Trawick:
We typically say when you start profiting around 50 to 75K, that's usually where we start saying, "Okay. Now, you could probably afford to pay yourself a salary. The administrative burden when you have to invest in other people to support that, whether it's administrative or operations staff to actually carry it out, an attorney that's helping you set all of that up." Like, we will file on your behalf for the IRS, but all states treat it differently, so you're going to need legal help for that, you're going to have to pay for a separate tax return, which can get expensive. And so, we just want to make sure that at that point you want to start at least thinking about it. And then, as a business owner, you want to consider whether or not that is realistic for you to sustain.

So, if you're making $50,000 this year, do you think that you're going to make $10,000 next year, because it's always this wide variance while you can elect and de-elect S-Corp? Relatively frequently, it's not something that you want to keep doing because the IRS will inevitably mess that up for you.

Sam Vander Wielen:
Yeah, yeah, that's really good advice. All right. Thank you. Oh, my goodness. This was all so helpful. If you have a minute, I was going to ask you, I have a little Would You Rather Game that I like to play at the end.

Keila Hill-Trawick:
Yes. I am in.

Sam Vander Wielen:
All right. So, first up is, would you rather read fiction or nonfiction?

Keila Hill-Trawick:

It’s always fiction. Even though I keep saying that I want to read more nonfiction, it’s always fiction.

Sam Vander Wielen:
I find it really helpful to unplug and read fiction, like get away from business stuff. Have you read anything good lately?

Keila Hill-Trawick:
Right now, I’m reading Rest Is Resistance, which is actually nonfiction. A book that I keep thinking about that I really loved from last year was The Invisible Life of Addie LaRue.

Sam Vander Wielen:
I remember seeing that. It was good.

Keila Hill-Trawick:
That was so good. And The Seven Husbands of Evelyn Hugo.

Sam Vander Wielen:
Evelyn Hugo, that was really good. Yeah. That was really good. I liked that a lot too. Okay, that’s a good one. Would you rather live at the beach, the mountains, or the desert?

Keila Hill-Trawick:
Oh, the beach.

Sam Vander Wielen:
Same.

Keila Hill-Trawick:
I am a water, like anytime I can be close to the water, I want to be.

Sam Vander Wielen:
Yeah. You and me both. Would you rather order coffee or tea?

Keila Hill-Trawick:

Coffee. I just discovered coffee, like, last year. I couldn't have it for a long time because I had a caffeine sensitivity, which I think I just overrode in my body. And now I have it every day. I'm like, I cannot believe that I missed out on coffee all this time until 2021.

Sam Vander Wielen:
How were you functioning? Oh, my goodness.

Keila Hill-Trawick:
Water. And it is not the same.

Sam Vander Wielen:
I know, right? Not the same. So, do you have a go-to coffee order now that you've been able to discover it?

Keila Hill-Trawick:
I drink a lot of mocha lattes, which I realized is just hot chocolate with coffee in it, and that's probably why I think it's delicious. But, yes, I drink a ton of those.

Sam Vander Wielen:
That's amazing. Yeah. Okay. This is a very controversial one, would you rather clean up as you go or clean up at the end when you cook?

Keila Hill-Trawick:
I would rather clean up as I go. I am not though. I'm always going to clean up at the end.

Sam Vander Wielen:
People have said that this causes a lot of marital strife in their relationship.

Keila Hill-Trawick:
So, I am very lucky because I don't cook our meals. My husband cooks our meals. So, what typically happens is that he cooks, and then if I'm doing what I'm supposed to do, I clean up.

Sam Vander Wielen:
You clean. Yeah. That's our bounce. But the opposite, I cook everything. He cleans, which is nice. But I do like to clean up as I go because as I cook, it drives me a little nuts when things are really messy in my work station. So, I kind of clean up a little or if I have downtime. But, yeah, that's really funny. One of my friends, her and her husband had to come to an agreement about cleaning up as they go, it's so funny. It's controversial.

Keila Hill-Trawick:
My husband says I leave things in my wake, so I tend to start things and then just walk off. And then, I'll come back later, I'm like, "Why is there so much stuff all over?" He's like, "Because you started. You decided you were going to make biscuits, you started the process, your phone rang or something happened, and you left. And now all of the ingredients are still here just laying out because you did not complete it. [Inaudible] the cleaner." Because I just come down and do that whenever I get ready.

Sam Vander Wielen:
Yeah, that was really funny, the Keila trail. All right. Last but not least, would you rather hit up a fancy restaurant or the best food trucks?

Keila Hill-Trawick:
So, I'm very into spoiling myself as of late, and I think that luxury restaurants always just felt out of reach for me where I was like, "Why would I spend that much when I could do this?" And so, as I have had more experiences in really nice restaurants, I very much appreciate the intentionality that comes with it. So, I like both, but I have experienced enough food trucks and not enough luxury restaurants.

Sam Vander Wielen:
Yeah. You got to give it a go. There's so many where you live, so many places to go, that's awesome.

Keila Hill-Trawick:
Yeah. I have a lot to try.

Sam Vander Wielen:

Yeah, so many. Well, I so appreciate this conversation. I know everybody's going to find it so helpful. Would you tell everybody how to reach out to you and any next steps in case they want to work with you and Little Fish.

Keila Hill-Trawick:
Yeah, absolutely. So, you can find everything that we have online on our website at littlefishaccounting.com. We are most active on Instagram, @littlefishaccounting. I'm trying to get better at LinkedIn, so we're over there too. I'm not nearly as good at it, but I try.

And then, in terms of services, we have the Tax Prep Suite for which the doors are open right now. You can go to littlefishaccounting.com/services, that is going to cover the entire next year of taxes. So, January through December estimated taxes, annual taxes, tax planning calls, webinars, all of that to really get taxes out of your way. And then, we have three monthly service tiers that you can learn more about on the website just based on where your business is and what feels most pressing to you.

Sam Vander Wielen:
That's awesome. Thank you so much, Keila. I so appreciate you. Thanks for being here.

Keila Hill-Trawick:
Thank you for having me. I appreciate you asking me and I'm glad that I could provide some value to the group.

Sam Vander Wielen:
Of course. So much value.

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