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Guide · S corps & entities 12 min read

The Complete S Corp Election Guide for 2026

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Updated September 29, 2026 · Written for self-employed owners and single-member LLCs earning $80k+

The short answer

An S corp election lets an owner split business profit into a salary (subject to payroll tax) and distributions (not subject to self-employment tax). Once you count the QBI deduction you give up and the roughly $2,500–$4,000 a year it costs to run payroll and file a separate return, it usually starts to pay meaningfully when net profit is consistently above about $100,000. Between $60,000 and $100,000 it's often close to break-even. For a calendar-year business, Form 2553 is due by March 15 of the year you want it to start.

What an S corp election actually is

An S corporation isn't a different kind of company you form. It's a tax election, filed on Form 2553, that an LLC or corporation makes to be taxed under Subchapter S. Your LLC stays an LLC legally. Only the tax treatment changes.

By default, a single-member LLC is taxed like a sole proprietorship. All of its net profit is subject to self-employment tax of 15.3% on 92.35% of earnings, up to the 2026 Social Security wage base of $184,500, and 2.9% above it. With an S election, you become an employee of your own company. Payroll tax applies to your salary, and the remaining profit comes to you as a distribution without self-employment tax.

The 2026 math at five profit levels

These figures compare a single filer's total federal tax as a sole proprietor versus an S corp, including the change in the QBI deduction. Salaries are set at a defensible level for each profit, and neither case is a specified service

business. The last column is the number that matters.

Net profit	S corp salary	Sole prop SE tax	S corp payroll tax	Savings before costs	Savings after $3,000 costs
$60,000	$35,000	$8,478	$5,355	$2,519	−$193
$80,000	$45,000	$11,304	$6,885	$3,138	$666
$120,000	$60,000	$16,955	$9,180	$5,160	$2,688
$200,000	$90,000	$28,234	$13,770	$9,529	$7,105
$300,000	$120,000	$30,912	$18,360	$20,331	$18,099

The last column takes out $3,000 a year for the 1120-S return, payroll software and state unemployment tax. Those costs are deductible, so they reduce savings by a little less than $3,000. The payroll tax saved looks large, but two things eat into it: your salary and the running costs both shrink the 20% QBI deduction. At $60,000 of profit the election loses money, and at $80,000 it saves about $55 a month. At $300,000 the savings jump because the S corp's W-2 wages let the owner keep the QBI deduction above the income threshold, which a sole proprietor without employees can lose.

> Your numbers will differ with filing status, other income, state tax and whether your business is a specified service business. Run them in the S corp savings calculator.

Reasonable compensation: the rule that makes or breaks it

The IRS requires S corp owners who work in the business to pay themselves a reasonable salary before taking distributions. Setting salary too low is the most common way S corps get into trouble, because the IRS can reclassify distributions as wages and assess back payroll tax, penalties and interest.

Reasonable means what you would have to pay someone else to do the work you do. Good support includes:

- Salary survey or Bureau of Labor Statistics data for your role and region
- The hours you work and the duties you perform
- What comparable businesses pay for similar roles
- A written memo in your files explaining how the number was set

There's no safe percentage. A 60/40 split is only a rule of thumb. Salary also affects your QBI deduction and your retirement contributions, so the right number balances all three.

How the election interacts with the QBI deduction

The Qualified Business Income deduction under Section 199A lets eligible owners deduct up to 20% of business income. The One Big Beautiful Bill Act made it permanent. In an S corp, your salary is not QBI; only the distribution is. A higher salary therefore lowers QBI.

Above the 2026 taxable income thresholds of $201,750 (single) and $403,500 (married filing jointly), the deduction phases toward a limit of 50% of W-2 wages paid. That's where an S corp can help: your own salary counts as W-2 wages. The phase-in range is $75,000 for single filers and $150,000 for joint filers in 2026.

Specified service businesses such as consulting, health, law, accounting and financial services lose the deduction entirely once taxable income passes the top of the phase-in range.

Retirement contributions inside an S corp

As an S corp owner, your retirement plan contributions are based on your W-2 salary. Distributions don't count. For 2026 the Solo 401(k) employee deferral is $24,500, the employer contribution is up to 25% of salary, and total additions are capped at $72,000, plus catch-up contributions of $8,000 at age 50 or older, or $11,250 at ages 60 to 63.

If saving aggressively for retirement matters to you, that can justify a higher salary than you would otherwise choose.

State taxes that change the answer

- California charges S corps a 1.5% franchise tax on net income, with an $800 minimum.
- New York City does not recognize the S election for its general corporation tax.
- Several states tax S corps or impose gross receipts or franchise taxes of their own.
- Many states offer a pass-through entity tax (PTET) election that can work around the federal SALT cap, and it's often only available to S corps and partnerships.

How and when to file Form 2553

- File within two months and 15 days after the start of the tax year the election should take effect. For a calendar year, that's March 15, or the next business day. For 2027, it's Monday, March 15, 2027.

Every shareholder must sign. An eligible LLC doesn't need a separate Form 8832: a timely Form 2553 also elects corporate classification.

If you miss the deadline, relief is often available under Rev. Proc. 2013-30 with a reasonable-cause statement.

Set up payroll before your first distribution, and run it at least quarterly.

Costs that don't show up on the tax bill

Lower Social Security credits: less income is taxed for Social Security, so your future benefit is based on a lower salary.

Smaller retirement contributions: employer contributions are 25% of W-2 salary only, versus about 20% of your full profit as a sole proprietor.

Payroll every month or quarter, state unemployment accounts and a separate corporate return, plus the time they take.

Reasonable-salary risk: if the IRS decides your salary is too low, it can reclassify distributions as wages and assess back payroll tax.

Five years to change your mind: if you revoke the election, you generally can't elect again for five years.

Should you elect?

Stay a default LLC if…	Consider an S corp if…
Net profit is under about $80,000	Profit is consistently above about $100,000
Income swings widely year to year	Income is stable and predictable
The business is losing money	You're the primary person doing the work
You value simplicity above all	You'll keep clean books and run payroll

Frequently asked questions

At what income does an S corp make sense in 2026?

Usually once net profit is consistently above about $100,000 a year. Below that, the QBI deduction you give up and the $2,500–$4,000 annual cost of payroll and a separate return eat most of the payroll tax savings. At $60,000 of profit, a single filer typically comes out behind.

When is the S corp election deadline for 2027?

For a calendar-year business, Form 2553 is due by Monday, March 15, 2027, which is two months and 15 days after the start of the tax year. Late election relief is often available under Rev. Proc. 2013-30.

How do I set a reasonable salary?

Base it on what you'd pay someone else to do your job: salary surveys, BLS data, your hours and duties. Document the method in writing. There is no safe percentage of profit.

General information based on federal law for tax year 2026, not tax advice for your situation. State rules vary.

Want this applied to your situation? Book a free 30-minute call with Akanchya Acharya, CPA at acharyacpa.com/contact or email akansha@acharyacpa.com.

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