Understanding Common Business Terms:
Gross Sales, Net Income, Owner's Draw and Owner's Equity
Jim Huston, Venture Mentors, LLC

The following business terms all represent distinctly different concepts, but are sometimes used incorrectly as interchangeable terms. Each of these concepts is different from the others and will generally represent significantly different amounts within a business.

Gross Sales is the amount that a business takes in from sales of products and/or services. This is also called "gross income" or sometimes "gross receipts". Gross sales does not represent the amount taxable by the Federal Government. It is also not the amount reported on the Work Activity Report to Social Security or the amount used to determine use of TWP months or SGA. For SSA purposes, the gross sales or gross income figure is not relevant in and of itself

Net Income is the amount of profit that the business makes. This number is derived by taking the gross sales and subtracting any legitimate expenses that the business incurred. The net income of a business is taxable and is reported to SSA on the Work Activity Report. This is the money available to the owner to draw or to expand the business. This profit is attributable to the business owner and is taxable, whether the owner actually draws it out and spends it or not. SSA uses net income from self-employment or NESE to decide whether or not TWP months had been used, and when making SGA determinations. NESE may be further reduced for SGA purposes by deducting any work incentives.

Owner's Draw is the amount of cash, goods or services that an owner takes out of the business. The draw can be less than net income, or it can be more. If a draw is less than net income, the "equity", or value of ownership increases. If a draw is more than net income, the equity or value of ownership decreases. Whatever relationship owner's draw has to net income is not important, because the draw is against owner's equity, not against net income. Net Income is all that is reportable to either the IRS or the SSA. Owner's draw is not a "salary" in the way this word usually is applied. The amount of money a business owner chooses to take out of the business is NOT relevant when SSA is making TWP or SGA determinations. These determinations depend entirely upon net earnings!

Owner's Equity is the amount of money invested in a business. This investment can be comprised of personal funds, State Vocational Rehabilitation funds, other State grants, PASS or other investments. Net income (or net loss) is added to the owner's equity each month, so an equity balance is maintained. Owner's draws are deducted from the equity balance as funds are paid out to the owner. The more net income an owner leaves in the business, the higher the owner's equity becomes.

708 Cherokee Woods Rd., Louisville, KY 40206 PH:502.930.2079 Fax: 502.896.6876 www.venturementors.biz