

within the meaning of paragraph (a) of § 1.1402(a)-13 (for example, the business of ordinary farming and the business of cotton ginning), the gross income derived from each agricultural trade or business shall be aggregated for purposes of the optional method provided in paragraph (a) of this section for computing net earnings from self-employment.

(d) *Examples.* Application of the regulations prescribed in paragraphs (a) and (b) of this section may be illustrated by the following examples:

*Example (1).* F, a farmer, uses the cash receipts and disbursements method of accounting in making his income tax returns. F's books and records show that during the calendar year 1955 he received \$1,200 from the sale of produce raised on the farm, \$200 from the sale of livestock raised on the farm and not held for breeding or dairy purposes, and \$600 from the sale of a tractor. The income from the sale of the tractor is of a type which is excluded from net earnings from self-employment by section 1402(a). F's actual net earnings from self-employment, computed in accordance with the provisions of §§ 1.1402(a)-1 through 1.1402(a)-3, are \$450. F may report \$450 as his net earnings from self-employment or he may elect to report \$700 (one-half of \$1,400).

*Example (2).* C, a cattleman, uses the cash receipts and disbursements method of accounting in making his income tax returns. C had actual net earnings from self-employment, computed in accordance with the provisions of §§ 1.1402(a)-1 through 1.1402(a)-3, of \$725. His gross receipts were \$1,000 from the sale of produce raised on the farm and \$1,200 from the sale of feeder cattle, which C bought for \$500. The income from the sale of the feeder cattle is of a type which is included in computing net earnings from self-employment. Therefore, C may report \$725 as his net earnings from self-employment or he may elect to report \$850, one-half of \$1,700 (\$2,200 minus \$500).

*Example (3).* R, a rancher, has gross income of \$3,000 from the operation of his ranch, computed as provided in paragraph (b) of this section. His actual net earnings from self-employment from farming activities are less than \$900. R, nevertheless, may elect to report \$900 as net earnings from self-employment from such trade or business. If R had actual net earnings from self-employment from his farming activities in the amount of \$900 or more, he would be required to report such amount in computing his self-employment income.

(e) *Members of farm partnerships.* The optional method provided by paragraph

(a) of this section for computing net earnings from self-employment is not available to a member of a partnership with respect to his distributive share of the income or loss from any trade or business carried on by any partnership of which he is a member.

**§ 1.1402(a)-15 Options available to farmers in computing net earnings from self-employment for taxable years ending on or after December 31, 1956.**

(a) *Computation of net earnings.* In the case of any trade or business which is carried on by an individual or by a partnership and in which, if such trade or business were carried on exclusively by employees, the major portion of the services would constitute agricultural labor as defined in section 3121(g) (see paragraph (a) of § 1.1402(a)-13), net earnings from self-employment may, for a taxable year ending on or after December 31, 1956, at the option of the taxpayer, be computed as follows:

(1) *In case of an individual—(i) Gross income of less than specified amount.* If the gross income, computed as provided in paragraph (b) of this section, from such trade or business is \$2,400 or less (\$1,800 or less for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966), the taxpayer may, at his option, treat as net earnings from self-employment from such trade or business an amount equal to 66⅔ percent of such gross income. If the taxpayer so elects, the amount equal to 66⅔ percent of such gross income shall be used in computing his self-employment income in lieu of his actual net earnings from such trade or business, if any.

(ii) *Gross income in excess of specified amount.* If the gross income, computed as provided in paragraph (b) of this section, from such trade or business is more than \$2,400 (\$1,800 for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966), and the net earnings from self-employment from such trade or business (computed without regard to this section) are less than \$1,600 (\$1,200 for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966), the taxpayer may, at his option, treat \$1,600 (\$1,200 for a taxable year ending on or after December 31,

1956, and beginning before January 1, 1966) as net earnings from self-employment. If the taxpayer so elects, \$1,600 (\$1,200 for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966) shall be used in computing his self-employment income in lieu of his actual net earnings from such trade or business, if any. However, if the taxpayer's actual net earnings from such trade or business, as computed in accordance with the applicable provisions of §§ 1.1402(a)-1 to 1.1402(a)-13, inclusive, are \$1,600 or more (\$1,200 or more for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966) such actual net earnings shall be used in computing his self-employment income.

(2) *In case of a member of a partnership*—(i) *Distributive share of gross income of less than specified amount.* If a taxpayer's distributive share of the gross income of a partnership (as such gross income is computed under the provisions of paragraph (b) of this section) derived from such trade or business (after such gross income has been reduced by the sum of all payments to which section 707(c) applies) is \$2,400 or less (\$1,800 or less for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966), the taxpayer may, at his option, treat as his distributive share of income described in section 702(a)(9) derived from such trade or business an amount equal to 66⅔ percent of his distributive share of such gross income (after such gross income has been reduced by the sum of all payments to which section 707(c) applies). If the taxpayer so elects, the amount equal to 66⅔ percent of his distributive share of such gross income shall be used by him in the computation of his net earnings from self-employment in lieu of the actual amount of his distributive share of income described in section 702(a)(9) from such trade or business, if any.

(ii) *Distributive share of gross income in excess of specified amount.* If a taxpayer's distributive share of the gross income of the partnership (as such gross income is computed under the provisions of paragraph (b) of this section) derived from such trade or business (after such gross income has been

reduced by the sum of all payments to which section 707(c) applies) is more than \$2,400 (\$1,800 for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966) and the actual amount of his distributive share (whether or not distributed) of income described in section 702(a)(9) derived from such trade or business (computed without regard to this section) is less than \$1,600 (\$1,200 for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966), the taxpayer may, at his option, treat \$1,600 (\$1,200 for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966) as his distributive share of income described in section 702(a)(9) derived from such trade or business. If the taxpayer so elects, \$1,600 (\$1,200 for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966) shall be used by him in the computation of his net earnings from self-employment in lieu of the actual amount of his distributive share of income described in section 702(a)(9) from such trade or business, if any. However, if the actual amount of the taxpayer's distributive share of income described in section 702(a)(9) from such trade or business, as computed in accordance with the applicable provisions of §§ 1.1402(a)-1 to 1.1402(a)-13, inclusive, is \$1,600 or more (\$1,200 or more for a taxable year ending on or after December 31, 1956, and beginning before January 1, 1966), such actual amount of the taxpayer's distributive share shall be used in computing his net earnings from self-employment.

(iii) *Cross reference.* For a special rule in the case of certain deceased partners, see paragraph (c) of § 1.1402(f)-1.

(b) *Computation of gross income.* For purposes of this section gross income has the following meanings:

(1) In the case of any such trade or business in which the income is computed under a cash receipts and disbursements method, the gross receipts from such trade or business reduced by the cost or other basis of property which was purchased and sold in carrying on such trade or business (see paragraphs (a) and (c), other than paragraph (a)(5), of § 1.61-4, adjusted (after such reduction) in accordance with the

applicable provisions of §§ 1.1402(a)-3 to 1.1402(a)-13, inclusive.

(2) In the case of any such trade or business in which the income is computed under an accrual method (see paragraphs (b) and (c), other than paragraph (b)(5), of § 1.61-4), the gross income from such trade or business, adjusted in accordance with the applicable provisions of §§ 1.1402(a)-3 to 1.1402(a)-13, inclusive.

(c) *Two or more agricultural activities.* If an individual (including a member of a partnership) derives gross income (as defined in paragraph (b) of this section) from more than one agricultural trade or business, such gross income (including his distributive share of the gross income of any partnership derived from any such trade or business) shall be deemed to have been derived from one trade or business. Thus, such an individual shall aggregate his gross income derived from each agricultural trade or business carried on by him (which includes, under paragraph (b) of § 1.1402(a)-1, any guaranteed payment, within the meaning of section 707(c), received by him from a farm partnership of which he is a member) and his distributive share of partnership gross income (after such gross income has been reduced by any guaranteed payment within the meaning of section 707(c)) derived from each farm partnership of which he is a member. Such gross income is the amount to be considered for purposes of the optional method provided in this section for computing net earnings from self-employment. If the aggregate gross income of an individual includes income derived from an agricultural trade or business carried on by him and a distributive share of partnership income derived from an agricultural trade or business carried on by a partnership of which he is a member, such aggregate gross income shall be treated as income derived from a single trade or business carried on by him, and such individual shall apply the optional method applicable to individuals set forth in paragraph (a)(1) of this section for purposes of computing his net earnings from self-employment.

(d) *Examples.* The application of this section may be illustrated by the following examples:

*Example (1).* F is engaged in the business of farming and computes his income under the cash receipts and disbursements method. He files his income tax returns on the basis of the calendar year. During the year 1966, F's gross income from the business of farming (computed in accordance with paragraph (b) (1) of this section) is \$2,325. His actual net earnings from self-employment derived from such business are \$1,250. As his net earnings from self-employment, F may report \$1,250 or, by the optional computation method, he may report \$1,550 (66⅔ percent of \$2,325).

*Example (2).* G is engaged in the business of farming and computes his income under the accrual method. His income tax returns are filed on the calendar year basis. For the year 1966, G's gross income from the operation of his farm (computed in accordance with paragraph (b)(2) of this section) is \$2,800. He has actual net earnings from self-employment derived from such farm in the amount of \$1,250. As his net earnings from self-employment derived from his farm, G may report his actual net earnings of \$1,250, or by the optional method he may report \$1,600. If G's actual net earnings from self-employment from his farming activities for 1966 were in an amount of \$1,600 or more, he would be required to report such amount in computing his self-employment income.

*Example (3).* M, who files his income tax returns on a calendar year basis, is one of the three partners of the XYZ Company, a partnership, engaged in the business of farming. The taxable year of the partnership is the calendar year, and its income is computed under the cash receipts and disbursements method. For M's services in connection with the planting, cultivating, and harvesting of the crops during the year 1966 the partnership agrees to pay him \$500, the full amount of which is determined without regard to the income of the partnership and constitutes a guaranteed payment within the meaning of section 707(c). This guaranteed payment to M is the only such payment made during such year. The gross income derived from the business for the year 1966 computed in accordance with paragraph (b)(1) of this section and after being reduced by the guaranteed payment of \$500 made to M, is \$3,000. One-third of the \$3,000 (\$1,000), is M's distributive share of such gross income. Under paragraph (c) of this section, the guaranteed payment (\$500) received by M and his distributive share of the partnership gross income (\$1,000) are deemed to have been derived from one trade or business, and such amounts must be aggregated for purposes of the optional method of computing net earnings from self-employment. Since M's combined gross income from his two agricultural businesses (\$1,000 and \$500) is not more than \$2,400 and since such income is deemed to be derived from one trade or business, M's net earnings from self-employment derived from such

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farming business may, at his option, be deemed to be \$1,000 (66⅔ percent of \$1,500).

*Example (4).* A is one of the two partners of the AB partnership which is engaged in the business of farming. The taxable year of the partnership is the calendar year and its income is computed under the accrual method. A files his income tax returns on the calendar year basis. The partnership agreement provides for an equal sharing in the profits and losses of the partnership by the two partners. A is an experienced farmer and for his services as manager of the partnership's farm activities during the year 1966 he receives \$6,000 which amount constitutes a guaranteed payment within the meaning of section 707(c). The gross income of the partnership derived from such business for the year 1966, computed in accordance with paragraph (b)(2) of this section and after being reduced by the guaranteed payment made to A, is \$9,600. A's distributive share of such gross income is \$4,800 and his distributive share of income described in section 702(a)(9) derived from the partnership's business is \$1,900. Under paragraph (c) of this section, the guaranteed payment received by A and his distributive share of the partnership gross income are deemed to have been derived from one trade or business, and such amounts must be aggregated for purposes of the optional method of computing his net earnings from self-employment. Since the aggregate of A's guaranteed payment (\$6,000) and his distributive share of partnership gross income (\$4,800) is more than \$2,400 and since the aggregate of A's guaranteed payment (\$6,000) and his distributive share (\$1,900) of partnership income described in section 702(a)(9) is not less than \$1,600, the optional method of computing net earnings from self-employment is not available to A.

*Example (5).* F is a member of the EFG partnership which is engaged in the business of farming. F files his income tax returns on the calendar year basis. The taxable year of the partnership is the calendar year, and its income is computed under a cash receipts and disbursements method. Under the partnership agreement the partners are to share equally the profits or losses of the business. The gross income derived from the partnership business for the year 1966, computed in accordance with paragraph (b)(1) of this section is \$7,500. F's share of such gross income is \$2,500. Due to drought and an epidemic among the livestock, the partnership sustains a net loss of \$7,800 for the year 1966 of which loss F's share is \$2,600. Since F's distributive share of gross income derived from such business is in excess of \$2,400 and since F does not receive income described in section 702(a)(9) of \$1,600 or more from such business, he may, at his option, be deemed to have received \$1,600 as his distributive share

of income described in section 702(a)(9) from such business.

[T.D. 6691, 28 FR 12796, Dec. 3, 1963, as amended by T.D. 6993, 34 FR 828, Jan. 18, 1969]

### § 1.1402(a)-16 Exercise of option.

A taxpayer shall, for each taxable year with respect to which he is eligible to use the optional method described in § 1.1402(a)-14 or § 1.1402(a)-15, make a determination as to whether his net earnings from self-employment are to be computed in accordance with such method. If the taxpayer elects the optional method for a taxable year, he shall signify such election by computing net earnings from self-employment under the optional method as set forth in Schedule F (Form 1040) of the income tax return filed by the taxpayer for such taxable year. If the optional method is not elected at the time of the filing of the return for a taxable year with respect to which the taxpayer is eligible to elect such optional method, such method may be elected on an amended return (or on such other form as may be prescribed for such use) filed within the period prescribed by section 6501 and the regulations thereunder for the assessment of the tax for such taxable year. If the optional method is elected on a return for a taxable year, the taxpayer may revoke such election by filing an amended return (or such other form as may be prescribed for such use) for the taxable year within the period prescribed by section 6501 and the regulations thereunder for the assessment of the tax for such taxable year. If the taxpayer is deceased or unable to make an election, the person designated in section 6012(b) and the regulations thereunder may, within the period prescribed in this section elect the optional method for any taxable year with respect to which the taxpayer is eligible to use the optional method and revoke an election previously made by or for the taxpayer.

### § 1.1402(a)-17 Retirement payments to retired partners.

(a) *In general.* There shall be excluded, in computing net earnings from self-employment for taxable years ending on or after December 31, 1967, certain payments made on a periodic basis