

§ 1.1402(a)-1

26 CFR Ch. I (4-1-04 Edition)

<i>Taxable year</i>	<i>Percent</i>
Beginning after December 31, 1965 and before January 1, 1967 .....	0.35
Beginning after December 31, 1966 and before January 1, 1968 .....	.50
Beginning after December 31, 1967 and before January 1, 1973 .....	.60
Beginning after December 31, 1972 and before January 1, 1974 .....	1.0
Beginning after December 31, 1973 and before January 1, 1978 .....	.90
Beginning after December 31, 1977 and before January 1, 1981 .....	1.10
Beginning after December 31, 1980 and before January 1, 1986 .....	1.35
Beginning after December 31, 1985 .....	1.50

(c) In general, self-employment income consists of the net earnings derived by an individual (other than a nonresident alien) from a trade or business carried on by him as sole proprietor or by a partnership of which he is a member, including the net earnings of certain employees as set forth in § 1.1402(c)-3, and of crew leaders, as defined in section 3121(o) (see such section and the regulations thereunder in part 31 of this chapter (Employment Tax Regulations)). See, however, the exclusions, exceptions, and limitations set forth in §§ 1.1402(a)-1 through 1.1402(h)-1.

[T.D. 6993, 34 FR 828, Jan. 18, 1969, as amended by T.D. 7333, 39 FR 44445, Dec. 24, 1974]

**§ 1.1402(a)-1 Definition of net earnings from self-employment.**

(a) Subject to the special rules set forth in §§ 1.1402(a)-3 to 1.1402(a)-17, inclusive, and to the exclusions set forth in §§ 1.1402(c)-2 to 1.1402(c)-7, inclusive, the term “net earnings from self-employment” means:

(1) The gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by chapter 1 of the Code which are attributable to such trade or business, plus

(2) His distributive share (whether or not distributed), as determined under section 704, of the income (or minus the loss), described in section 702(a)(9) and as computed under section 703, from any trade or business carried on by any partnership of which he is a member.

(b) Gross income derived by an individual from a trade or business includes payments received by him from a partnership of which he is a member for services rendered to the partnership

or for the use of capital by the partnership, to the extent the payments are determined without regard to the income of the partnership. However, such payments received from a partnership not engaged in a trade or business within the meaning of section 1402(c) and § 1.1402(c)-1 do not constitute gross income derived by an individual from a trade or business. See section 707(c) and the regulations thereunder, relating to guaranteed payments to a member of a partnership for services or the use of capital. See also section 706(a) and the regulations thereunder, relating to the taxable year of the partner in which such guaranteed payments are to be included in computing taxable income.

(c) Gross income derived by an individual from a trade or business includes gross income received (in the case of an individual reporting income on the cash receipts and disbursements method) or accrued (in the case of an individual reporting income on the accrual method) in the taxable year from a trade or business even though such income may be attributable in whole or in part to services rendered or other acts performed in a prior taxable year as to which the individual was not subject to the tax on self-employment income.

[T.D. 6691, 28 FR 12796, Dec. 3, 1963, as amended by T.D. 7333, 39 FR 44445, Dec. 24, 1974]

**§ 1.1402(a)-2 Computation of net earnings from self-employment.**

(a) *General rule.* In general, the gross income and deductions of an individual attributable to a trade or business (including a trade or business conducted by an employee referred to in paragraphs (b), (c), (d), or (e) of § 1.1402(c)-3), for the purpose of ascertaining his net earnings from self-employment, are to be determined by reference to the provisions of law and regulations applicable with respect to the taxes imposed by sections 1 and 3. Thus, if an individual uses the accrual method of accounting in computing taxable income from a trade or business for the purpose of the tax imposed by section 1 or 3, he must use the same method in determining net earnings from self-employment. Likewise, if a taxpayer engaged in a trade or business of selling

property on the installment plan elects, under the provisions of section 453, to use the installment method in computing income for purposes of the tax under section 1 or 3, he must use the same method in determining net earnings from self-employment. Income which is excludable from gross income under any provision of subtitle A of the Internal Revenue Code is not taken into account in determining net earnings from self-employment except as otherwise provided in §1.1402(a)-9, relating to certain residents of Puerto Rico, in §1.1402(a)-11, relating to ministers or members of religious orders, and in §1.1402(a)-12, relating to the term "possession of the United States" as used for purposes of the tax on self-employment income. Thus, in the case of a citizen of the United States conducting, in a foreign country, a trade or business in which both personal services and capital are material income-producing factors, any part of the income therefrom which is excluded from gross income as earned income under the provisions of section 911 and the regulations thereunder is not taken into account in determining net earnings from self-employment.

(b) *Trade or business carried on.* The trade or business must be carried on by the individual, either personally or through agents or employees. Accordingly, income derived from a trade or business carried on by an estate or trust is not included in determining the net earnings from self-employment of the individual beneficiaries of such estate or trust.

(c) *Aggregate net earnings.* Where an individual is engaged in more than one trade or business within the meaning of section 1402(c) and §1.1402(c)-1, his net earnings from self-employment consist of the aggregate of the net income and losses (computed subject to the special rules provided in §§1.1402(a)-1 to 1.1402(a)-17 inclusive) of all such trades or businesses carried on by him. Thus, a loss sustained in one trade or business carried on by an individual will operate to offset the income derived by him from another trade or business.

(d) *Partnerships.* The net earnings from self-employment of an individual include, in addition to the earnings

from a trade or business carried on by him, his distributive share of the income or loss, described in section 702(a)(9), from any trade or business carried on by each partnership of which he is a member. An individual's distributive share of such income or loss of a partnership shall be determined as provided in section 704, subject to the special rules set forth in section 1402(a) and in §§1.1402(a)-1 to 1.1402(a)-17, inclusive, and to the exclusions provided in section 1402(c) and §§1.1402(c)-2 to 1.1402(c)-7, inclusive. For provisions relating to the computation of the taxable income of a partnership, see section 703.

(e) *Different taxable years.* If the taxable year of a partner differs from that of the partnership, the partner shall include, in computing net earnings from self-employment, his distributive share of the income or loss, described in section 702(a)(9), of the partnership for its taxable year ending with or within the taxable year of the partner. For the special rule in case of the termination of a partner's taxable year as result of death, see §§1.1402(f) and 1.1402(f)-1.

(f) *Meaning of partnerships.* For the purpose of determining net earnings from self-employment, a partnership is one which is recognized as such for income tax purposes. For income tax purposes, the term "partnership" includes not only a partnership as known at common law, but, also a syndicate, group, pool, joint venture, or other unincorporated organization which carries on any trade or business, financial operation, or venture, and which is not, within the meaning of the Code, a trust, estate, or a corporation. An organization described in the preceding sentence shall be treated as a partnership for purposes of the tax on self-employment income even though such organization has elected, pursuant to section 1361 and the regulations thereunder, to be taxed as a domestic corporation.

(g) *Nature of partnership interest.* The net earnings from self-employment of a partner include his distributive share of the income or loss, described in section 702(a)(9), of the partnership of which he is a member, irrespective of the nature of his membership. Thus, in determining his net earnings from self-

employment, a limited or inactive partner includes his distributive share of such partnership income or loss. In the case of a partner who is a member of a partnership with respect to which an election has been made pursuant to section 1361 and the regulations thereunder to be taxed as a domestic corporation, net earnings from self-employment include his distributive share of the income or loss, described in section 702(a)(9), from the trade or business carried on by the partnership computed without regard to the fact that the partnership has elected to be taxed as a domestic corporation.

(h) *Proprietorship taxed as domestic corporation.* A proprietor of an unincorporated business enterprise with respect to which an election has been made pursuant to section 1361 and the regulations thereunder to be taxed as a domestic corporation shall compute his net earnings from self-employment without regard to the fact that such election has been made.

[T.D. 6691, 28 FR 12796, Dec. 3, 1963, as amended by T.D. 7333, 39 FR 44445, Dec. 24, 1974]

**§ 1.1402(a)-3 Special rules for computing net earnings from self-employment.**

For the purpose of computing net earnings from self-employment, the gross income derived by an individual from a trade or business carried on by him, the allowable deductions attributable to such trade or business, and the individual's distributive share of the income or loss, described in section 702(a)(9), from any trade or business carried on by a partnership of which he is a member shall be computed in accordance with the special rules set forth in §§ 1.1402(a)-4 to 1.1402(a)-17, inclusive.

[T.D. 7333, 39 FR 44445, Dec. 24, 1974]

**§ 1.1402(a)-4 Rentals from real estate.**

(a) *In general.* Rentals from real estate and from personal property leased with the real estate (including such rentals paid in crop shares) and the deductions attributable thereto, unless such rentals are received by an individual in the course of a trade or business as a real-estate dealer, are excluded. Whether or not an individual is

engaged in the trade or business of a real-estate dealer is determined by the application of the principles followed in respect of the taxes imposed by sections 1 and 3. In general, an individual who is engaged in the business of selling real estate to customers with a view to the gains and profits that may be derived from such sales is a real-estate dealer. On the other hand, an individual who merely holds real estate for investment or speculation and receives rentals therefrom is not considered a real-estate dealer. Where a real-estate dealer holds real estate for investment or speculation in addition to real estate held for sale to customers in the ordinary course of his trade or business as a real-estate dealer, only the rentals from the real estate held for sale to customers in the ordinary course of his trade or business as a real-estate dealer, and the deductions attributable thereto, are included in determining net earnings from self-employment; the rentals from the real estate held for investment or speculation, and the deductions attributable thereto, are excluded. Rentals paid in crop shares include income derived by an owner or lessee of land under an agreement entered into with another person pursuant to which such other person undertakes to produce a crop or livestock on such land and pursuant to which (1) the crop or livestock, or the proceeds thereof, are to be divided between such owner or lessee and such other person, and (2) the share of the owner or lessee depends on the amount of the crop or livestock produced. See, however, paragraph (b) of this section.

(b) *Special rule for "includible farm rental income"*—(1) *In general.* Notwithstanding the rules set forth in paragraph (a) of this section, there shall be included in determining net earnings from self-employment for taxable years ending after 1955 any income derived by an owner or tenant of land, if the following requirements are met with respect to such income:

(i) The income is derived under an arrangement between the owner or tenant of land and another person which provides that such other person shall produce agricultural or horticultural commodities on such land, and that there shall be material participation