



Tax Reduction Letter

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Reg. Section 1.1402(b)-1

Self-employment income.

(a) In general. Except for the exclusions in paragraphs (b) and (c) of this section and the exception in paragraph (d) of this section, the term "self-employment income" means the net earnings from self-employment derived by an individual during a taxable year.

(b) Maximum self-employment income -- (1) General rule. Subject to the special rules described in subparagraph (2) of this paragraph, the maximum self-employment income of an individual for a taxable year (whether a period of 12 months or less) is:

(i) For any taxable year beginning in a calendar year after 1974, an amount equal to the contribution and benefit base (as determined under section 230 of the Social Security Act) which is effective for such calendar year; and

(ii) For any taxable year:

Ending before 1955 -- \$ 3,600

Ending after 1954 and before 1959 -- 4,200

Ending after 1958 and before 1966 -- 4,800

Ending after 1965 and before 1968 -- 6,600

Ending after 1967 and beginning before 1972 -- 7,800

Beginning after 1971 and before 1973 -- 9,000

Beginning after 1972 and before 1974 -- 10,800

Beginning after 1973 and before 1975 -- 13,200

(2) Special rules. (i) If an individual is paid wages as defined in subparagraph (3) of this paragraph in a taxable year, the maximum self-employment income for such taxable year is computed as provided in subdivision (ii) or (iii) of this subparagraph.

(ii) If an individual is paid wages as defined in subparagraph (3) (i) or (ii) of this paragraph in a taxable year, the maximum self-employment income of such individual for such taxable year is the excess of the amounts indicated in subparagraph (1) of this paragraph over the amount of the wages, as defined in subparagraph (3) (i) and (ii) of this paragraph, paid to him during the taxable year. For example, if for his taxable year beginning in 1974, an individual has \$ 15,000 of net earnings from self-employment and during such taxable year is paid \$ 1,000 of wages as defined in section 3121(a) [26 USCS § 3121(a)] (see subparagraph (3)(i) of this paragraph), he has \$ 12,200 (\$ 13,200 - \$ 1,000) of self-employment income for the taxable year.

(iii) For taxable years ending on or after December 31, 1968, wages, as defined in subparagraph (3)(iii) of this paragraph, are taken into account in determining the maximum self-employment income of an individual for purposes of the tax imposed under section 1401(b) [26 USCS § 1401(b)] (hospital insurance), but not for purposes of the tax imposed under section 1401(a) [26 USCS § 1401(a)] (old-age survivors, and disability insurance). If an individual is

paid wages as defined in subparagraph (3)(iii) of this paragraph in a taxable year, his maximum self-employment income for such taxable year for purposes of the tax imposed under section 1401(a) is computed under subparagraph (1) of this paragraph or subdivision (ii) of this subparagraph (whichever is applicable), and his maximum self-employment income for such taxable year for purposes of the tax imposed under section 1401(b) is the excess of his section 1401(a) maximum self-employment income over the amount of wages, as defined in subparagraph (3)(iii) of this paragraph, paid to him during the taxable year. For purposes of this subdivision, wages as defined in subparagraph (3)(iii) of this paragraph are deemed paid to an individual in the period with respect to which the payment is made, that is, the period in which the compensation was earned or deemed earned within the meaning of section 3231(e). For an explanation of the term "compensation" and for provisions relating to when compensation is earned, see the regulations under section 3231(e) in Part 31 of this chapter (Employment Tax Regulations). The application of the rules set forth in this subdivision may be illustrated by the following example:

Example. M, a calendar-year taxpayer, has \$ 15,000 of net earnings from self-employment for 1974 and during the taxable year is paid \$ 1,000 of wages as defined in section 3121(a) [26 USCS § 3121(a)] (see subparagraph (3)(i) of this paragraph) and \$ 1,600 of compensation subject to tax under section 3201 (see subparagraph (3)(iii) of this paragraph). Of the \$ 1,600 of taxable compensation, \$ 1,200 represents compensation for services rendered in 1974 and the balance (\$ 400) represents compensation which pursuant to the provisions of section 3231(e) is earned or deemed earned in 1973. M's maximum self-employment income for 1974 for purposes of the tax imposed under section 1401(a), computed as provided in subdivision (ii) of this subparagraph, is \$ 12,200 (\$ 13,200 - \$ 1,000), and for purposes of the tax imposed under section 1401(b) is \$ 11,000 (\$ 12,200 - \$ 1,200). However, M may recompute his maximum self-employment income for 1973 for purposes of the tax imposed under section 1401(b) by taking into account the \$ 400 of compensation which is deemed paid in 1973.

(3) Meaning of term "wages". For the purpose of the computation described in subparagraph (2) of this paragraph, the term "wages" includes:

(i) Wages as defined in section 3121(a);

(ii) Such remuneration paid to an employee for services covered by:

(a) An agreement entered into pursuant to section 218 of the Social Security Act (42 U.S.C. 418), which section provides for extension of the Federal old-age, survivors and disability insurance system to State and local government employees under voluntary agreements between the States and the Secretary of Health, Education, and Welfare (Federal Security Administrator before April 11, 1953), or

(b) An agreement entered into pursuant to the provisions of section 3121(1), relating to coverage of citizens of the United States who are employees of foreign subsidiaries of domestic corporations,

as would be wages under section 3121(a) if such services constituted employment under section 3121(b). For an explanation of the term "wages", see the regulations under section 3121(a) in Part 31 of this chapter (Employment Tax Regulations); and

(iii) Compensation, as defined in section 3231(e), which is subject to the employee tax imposed by section 3201 or the employee representative tax imposed by section 3211.

(c) Minimum net earnings from self-employment. Self-employment income does not include the net earnings from self-employment of an individual when the amount of such earnings for the

taxable year is less than \$ 400. Thus, an individual having only \$ 300 of net earnings from self-employment for the taxable year would not have any self-employment income. However, an individual having net earnings from self-employment of \$ 400 or more for the taxable year may, by application of paragraph (b)(2) of this section, have less than \$ 400 of self-employment income for purposes of the tax imposed under section 1401(a) and the tax imposed under section 1401(b) or may have self-employment income of \$ 400 or more for purposes of the tax imposed under section 1401(a) and of less than \$ 400 for purposes of the tax imposed under section 1401(b). This could occur in a case in which the amount of the individual's net earnings from self-employment is \$ 400 or more for a taxable year and the amount of such net earnings from self-employment plus the amount of wages, as defined in paragraph (b)(3) of this section, paid to him during the taxable year exceed the maximum self-employment income, as set forth in paragraph (b)(1) of this section, for the taxable year. However, the result occurs only if such maximum self-employment income exceeds the amount of such wages. The application of this paragraph may be illustrated by the following example:

Example. For 1974 M, a calendar-year taxpayer, has net earnings from self-employment of \$ 2,000 and wages (as defined in paragraph (b)(3) (i) and (ii) of this section) of \$ 12,500. Since M's net earnings from self-employment plus his wages exceed the maximum self-employment income for 1974 (\$ 13,200), his self-employment income for 1974 is \$ 700 (\$ 13,200 - \$ 12,500). If M also had wages, as defined in paragraph (b)(3)(iii) of this section, of \$ 200, his self-employment income would be \$ 700 for purposes of the tax imposed under section 1401(a) [26 USCS § 1401(a)] and \$ 500 (\$ 13,200 - \$ 12,700 (\$ 12,500+\$ 200)) for purposes of the tax imposed under section 1401(b).

For provisions relating to when wages as defined in paragraph (b)(3)(iii) of this section are treated as paid, see paragraph (b)(2)(iii) of this section.

(d) Nonresident aliens. A nonresident alien individual never has self-employment income. While a nonresident alien individual who derives income from a trade or business carried on within the United States, Puerto Rico, the Virgin Islands, Guam, or American Samoa (whether by agents or employees, or by a partnership of which he is a member) may be subject to the applicable income tax provisions on such income, such nonresident alien individual will not be subject to the tax on self-employment income, since any net earnings which he may have from self-employment do not constitute self-employment income. For the purpose of the tax on self-employment income, an individual who is not a citizen of the United States but who is a resident of the Commonwealth of Puerto Rico, the Virgin Islands, or, for taxable years beginning after 1960, of Guam or American Samoa is not considered to be a nonresident alien individual.