

## LB&I International Practice Service Concept Unit

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Shelf	N/A	Individual Outbound	–	–
Volume	9	Jurisdiction to Tax	<b>Level 1 UIL</b>	9431
Part	9.3	Social Security / Self-Employment Taxes for U.S. Persons Abroad	<b>Level 2 UIL</b>	9431.03
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<b>Unit Name</b>	Self-Employment Taxes - U.S. Citizens and Resident Aliens Working Abroad
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# General Overview

## Self-Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad

- An individual is considered to be self-employed if he or she is a sole proprietor, independent contractor, partner in a partnership, member of a limited liability company (including a single member limited liability company that is disregarded for tax purposes), member of a qualified joint venture, or otherwise in business for him or herself.
- The Self-Employment Contributions Act (SECA) provides for taxes akin to the Federal Insurance Contributions Act (FICA) taxes that must be paid by wage earners. The purpose of both SECA and FICA taxes is to fund the Federal system of old-age, survivors, disability, and hospital insurance benefits provided under the Social Security Act and related laws. This is known as the Social Security tax. SECA and FICA taxes also include a hospital insurance tax component, known as the Medicare tax.
- Under SECA, all U.S. citizens and resident aliens who are self-employed are responsible for paying self-employment tax if their net earnings from self-employment equal or exceed \$400. The obligation to pay self-employment tax arises whether the self-employment activities occur within or without the United States and whether the individual resides within or without the United States during the period of self-employment. To determine whether the \$400 threshold is met, all self-employment income is taken into account even if it is not subject to income tax due to the foreign earned income exclusion.
- As a general rule, nonresident aliens are not subject to U.S. self-employment tax. However, if a self-employed individual performs services while a nonresident alien, and later receives payment for those services after becoming a resident alien, that income is subject to U.S. self-employment tax. In other words, the determination as to whether someone is liable for U.S. self-employment tax based on their U.S. resident status is made as of the date the income is received, not the date the services were provided (unless a Totalization Agreement provides otherwise).
- Additionally, a nonresident alien will be subject to U.S. self-employment tax if such taxation is provided for under a Totalization Agreement.
- Although the term “resident” is not defined, residency for SECA and FICA taxes is generally the same as residency for income tax purposes.

# Relevant Key Factors

## Self-Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad

### Key Factors

- Generally, U.S. citizens and resident aliens must pay self-employment tax on their net earnings from self-employment, if the net earnings from self-employment equal or exceed \$400.
- Self-employment tax consists of Social Security taxes and Medicare taxes. It does not consist of any other taxes that may be owed by a self-employed individual.
- The United States and foreign countries enter into Totalization Agreements which are meant to avoid the payment of Social Security taxes to two jurisdictions on the same wage or self-employment income.

# Detailed Explanation of the Concept

## Self-Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad

All U.S. citizens and resident aliens who are self-employed are responsible for paying self-employment tax if their net earnings from self-employment equal or exceed \$400, regardless of whether the self-employment activities occur within or without the United States and whether the individual resides within or without the United States during the period of self-employment.

Analysis	Resources
<ul style="list-style-type: none"> <li>▪ Individuals must pay self-employment tax if they:               <ul style="list-style-type: none"> <li>- Are a U.S. citizen or resident alien,</li> <li>- Have net earnings from self-employment and</li> <li>- The net earnings from self-employment equal or exceed \$400.</li> </ul> </li>   <li>▪ Totalization Agreements are entered into between the United States and some foreign countries to avoid the payment of Social Security taxes to two jurisdictions on the same income (from wages or self-employment). A list of countries with which the U.S. has Totalization Agreements can be found on <a href="http://irs.gov">irs.gov</a> and <a href="http://socialsecurity.gov">socialsecurity.gov</a>. If the U.S. has entered into a Totalization Agreement with the foreign country in which the self-employment income was earned, the terms of that agreement will govern whether self-employment taxes must be paid in the United States or to the foreign country.</li>   <li>▪ More specifically, under IRC 1401(c), where a Totalization Agreement is in place, self-employment tax is not owed to the United States if the terms of the agreement provide that the self-employment income is subject only to foreign Social Security taxes and is exempt from U.S. self-employment tax.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 1402(a)</li> <li>▪ Schedule SE and Instructions</li>   <li>▪ IRC 1402(a)(1) through (17)</li> <li>▪ IRC 1401(c)</li> <li>▪ IRC 1402(a)(11)</li> <li>▪ Social Security Amendments of 1983, P.L. 98-21, section 323</li> <li>▪ Pub. 54, Tax Guide for U.S. Citizens and Resident Aliens Abroad</li> </ul>

# Detailed Explanation of the Concept (cont'd)

## Self-Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad


All U.S. citizens and resident aliens who are self-employed are responsible for paying self-employment tax if their net earnings from self-employment equal or exceed \$400, regardless of whether the self-employment activities occur within or without the United States and whether the individual resides within or without the United States during the period of self-employment.

Analysis	Resources
<ul style="list-style-type: none"><li>▪ If a taxpayer resides in a Country with a Totalization Agreement, you must read the Agreement to determine if all qualifications have been met, and exactly what income is included or excluded by each Country. Further, some Agreements may have related separate agreements, and Social Security Administration (SSA) annotations which may assist in applying the Agreement's provisions.</li><li>▪ A taxpayer claiming an exemption from Social Security taxation in the United States based on a Totalization Agreement must request a certificate of coverage from the appropriate agency of the foreign country and attach said certificate to his or her tax return. If a certificate cannot be obtained from the foreign country, the taxpayer should request a statement from the U.S. Social Security Administration stating that his or her income is not covered by the U.S. Social Security system, and attach it to the tax return. Whether the taxpayer attaches a certificate from the foreign jurisdiction or the U.S. Social Security Administration, he or she should print "Exempt, see attached statement" on the line on the tax return for self-employment tax.</li><li>▪ It may be necessary to determine where an individual lived, and where the individual performed services, for multiple periods in the same tax year, because tax treatment can vary depending on those issues regardless of whether there is a Totalization Agreement.</li></ul>	<ul style="list-style-type: none"><li>▪ IRC 1401(c)</li><li>▪ Social Security Administration's (SSA's) International Program's website</li> <li>▪ Rev. Proc. 80-56</li><li>▪ Rev. Proc. 84-54</li><li>▪ Schedule SE and Instructions</li></ul>

# Detailed Explanation of the Concept (cont'd)

## Self-Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad

All U.S. citizens and resident aliens who are self-employed are responsible for paying self-employment tax if their net earnings from self-employment equal or exceed \$400, regardless of whether the self-employment activities occur within or without the United States and whether the individual resides within or without the United States during the period of self-employment.

Analysis	Resources
<p> <b>CAUTION:</b> If a taxpayer is claiming an exemption from Social Security taxation in the United States based on a Totalization Agreement, he or she must request a certificate of coverage from the appropriate agency of the foreign country and attach the certificate to his or her U.S. tax return. If a certificate cannot be obtained from the foreign country, the taxpayer should request a statement from the U.S. Social Security Administration stating that his or her income is not covered by the U.S. Social Security system, and attach it to the tax return. If the taxpayer attaches a certificate from the foreign jurisdiction or the U.S. Social Security Administration to his or her U.S. tax return, he or she should print “Exempt, see attached statement” on the line on the tax return for self-employment tax.</p>	<ul style="list-style-type: none"><li>▪ IRC 1401(c)</li><li>▪ Social Security Administration’s (SSA’s) International Program’s website</li><li>▪ Rev. Proc. 80-56</li><li>▪ Rev. Proc. 84-54</li><li>▪ Schedule SE and Instructions</li></ul>

# Examples of the Concept

## Self-Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad

### Examples

In 2014, Ms. X, who is a United States citizen and a bona fide resident of Country A, worked for Architectural Company in Country A as an architect. She received a salary of \$85,000 USD (United States Dollars), as well as an overseas cost of living allowance of \$15,000 USD. Mr. Z, her next-door neighbor in Country A, was planning an addition to his home. He asked Ms. X to draw up plans and oversee the project in her spare time. Ms. X spent her days working for Architectural Company and her evenings and weekends planning and overseeing Mr. Z's home addition. As agreed, he paid her \$200,000 USD. Of this, she spent \$35,000 USD on materials and another \$100,000 USD on subcontractors, netting a profit of \$65,000 USD on the project. She elected to exclude \$99,200 of foreign earned income, the maximum allowable for tax year 2014.

- Ms. X's gross income from self-employment is \$200,000 USD. Her salary and cost of living allowance are not included in gross income from self-employment.
- Ms. X's net income from self-employment, which is subject to SECA, is \$65,000 (gross income minus material and sub-contractor expenses).
- The \$99,200 of excluded foreign earned income does not reduce Ms. X's net income from self-employment.
- For details on calculating the foreign earned income exclusion, please see the Practice Units, "Calculating Foreign Earned Income Exclusion – Employee," DCN: JTO/P/09\_06\_05-12 (formerly JTO/9431.06\_12(2015)), and "Calculating Foreign Earned Income Exclusion – Self-Employed Individual," DCN: JTO/P/09\_06\_05-13 (formerly JTO/9431.06\_13(2015)).



# Training and Additional Resources

## Self-Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad

Type of Resource	Descriptions and/or Instructions for Accessing	References
BNA Tax Management Portfolio	<ul style="list-style-type: none"><li>▪ <i>BNA Tax Management Int'l Portfolios</i>: Foreign Income Series: Provisions Applicable to U.S. and Foreign Persons 6830-1st Sec. VIII: International SECA Rules</li></ul>	<ul style="list-style-type: none"><li>▪ BNA 6830-1st – TMFEDPORT No 6830 s VIII</li></ul>
BNA Tax Management Portfolio	<ul style="list-style-type: none"><li>▪ <i>BNA Tax Management Int'l Portfolios</i>: Foreign Income Series: Provisions Applicable to U.S. and Foreign Persons 6830-1st Sec. III: Social Security Totalization Agreements</li></ul>	<ul style="list-style-type: none"><li>▪ BNA 6830-1st – TMFEDPORT No 6830 s III</li></ul>

# Glossary of Terms and Acronyms

Term/Acronym	Definition
DCN	Document Control Number
FICA	Federal Insurance Contributions Act
IRC	Internal Revenue Code
SECA	Self-Employment Contributions Act
SSA	Social Security Administration
USD	United States Dollars

# Index of Related Issues

Issue	Associated UILs	References
Employment Taxes for U.S. Citizens and Resident Aliens Working Abroad	▪ 9431.04	▪ Practice Unit, “Employee Share of Employment Taxes – U.S. Citizens and Resident Aliens Working Abroad,” DCN:JTO/C/09_03-22
Calculating the Foreign Earned Income Exclusion for a Self-Employed Individual	▪ 9431.06	▪ Practice Unit, “Calculating Foreign Earned Income Exclusion – Self-Employed Individual,” DCN:JTO/P/09_06_05-13 (formerly JTO/9431.06_13(2015))