2011 Instructions for Schedule SE (Form 1040)

Self-Employment Tax

Use Schedule SE (Form 1040) to figure the tax due on net earnings from self-employment. The Social Security Administration uses the information from Schedule SE to figure your benefits under the social security program. This tax applies no matter how old you are and even if you are already getting social security or Medicare benefits.

Additional information. See Pub. 225 or Pub. 334.

What’s New

More information. The IRS has created a page on IRS.gov for information about Form 1040 and its instructions, at www.irs.gov/form1040. Information about any recent developments affecting Schedule SE will be posted on that page.

Maximum income subject to social security tax. The maximum amount of self-employment income subject to social security tax remains $106,800.

Deduction for self-employed health insurance. You can no longer reduce your net self-employment income by the amount of your self-employed health insurance deduction (from line 29 of Form 1040 or Form 1040NR).

SE tax rate. For 2011, the Old Age, Survivors, and Disability Insurance (OASDI) portion of the SE tax is reduced by 2%, from 12.4% to 10.4%. The Medicare (HI) portion of the SE tax remains 2.9%. As a result, the SE tax rate is reduced from 15.3% to 13.3%.

SE tax deduction. For 2011, the SE tax deduction is revised to reflect an employer’s equivalent portion of tax. Previously, the deduction was equal to one-half of self-employment tax.

General Instructions

Who Must File Schedule SE

You must file Schedule SE if:

- The amount on line 4 of Short Schedule SE or line 4c of Long Schedule SE is $400 or more, or
- You had church employee income of $108.28 or more. Income from services you performed as a minister or a member of a religious order is not church employee income. See Employees of Churches and Church Organizations.

Note. Even if you had a loss or a small amount of income from self-employment, it may be to your benefit to file Schedule SE and use either “optional method” in Part II of Long Schedule SE (discussed later).

Exception. If your only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner, see Ministers and Members of Religious Orders.

Who Must Pay Self-Employment (SE) Tax

Self-Employed Persons

You must pay SE tax if you had net earnings of $400 or more as a self-employed person. If you are in business (farm or non-farm) for yourself, you are self-employed.

You must also pay SE tax on your share of certain partnership income and your guaranteed payments. See Partnership Income or Loss, later.

Employees of Churches and Church Organizations

If you had church employee income of $108.28 or more, you must pay SE tax. Church employee income is wages you received as an employee (other than as a minister or member of a religious order) of a church or qualified church-controlled organization that has a certificate in effect electing an exemption from employer social security and Medicare taxes.

Ministers and Members of Religious Orders

In most cases, you must pay SE tax on salaries and other income for services you performed as a minister, a member of a religious order who has not taken a vow of poverty, or a Christian Science practitioner. But if you filed Form 4361 and received IRS approval, you will be exempt from paying SE tax on those net earnings. If you had no other income subject to SE tax, enter “Exempt—Form 4361” on Form 1040, line 56, or Form 1040NR, line 54. However, if you had other net earnings of $400 or more subject to SE tax, see line A at the top of Long Schedule SE.

If you have ever filed Form 2031 to elect social security coverage on your earnings as a minister, you cannot revoke that election.

If you must pay SE tax, include this income on either Short or Long Schedule SE, line 2. But do not report it on Long Schedule SE, line 5a; it is not considered church employee income. Also, include on line 2:

- The rental value of a home or an allowance for a home furnished to you (including payments for utilities), and
- The value of meals and lodging provided to you, your spouse, and your dependents for your employer’s convenience.

However, do not include on line 2:

- Retirement benefits you received from a church plan after retirement, or
- The rental value of a home or an allowance for a home furnished to you (including payments for utilities) after retirement.

If you were a duly ordained minister who was an employee of a church and you must pay SE tax, when figuring SE tax, subtract on line 2 allowable expenses from your self-employment earnings and attach an explanation. Please note that the unreimbursed employee business expenses that you incurred as an employee of the church are not allowable expenses for SE tax purposes, and are allowed only as an itemized deduction for income tax purposes.

If you were a U.S. citizen or resident alien serving outside the United States as a minister or member of a religious order and you must pay SE tax, you cannot reduce your net earnings by the foreign earned income exclusion or the foreign housing exclusion or deduction.

See Pub. 517 for details.

Members of Certain Religious Sects

If you have conscientious objections to social security insurance because of your membership in and belief in the teachings of a religious sect recognized as being in existence at all times since December 31, 1950, and which has provided a reasonable level of living for its dependent members,
you are exempt from SE tax if you received IRS approval by filing Form 4029. In this case, do not file Schedule SE. Instead, enter “Exempt—Form 4029” on Form 1040, line 56, or Form 1040NR, line 54. See Pub. 517 for details.

U.S. Citizens Employed by Foreign Governments or International Organizations
You must pay SE tax on income you earned as a U.S. citizen employed by a foreign government (or, in certain cases, by a wholly owned instrumentality of a foreign government or an international organization under the International Organizations Immunities Act) for services performed in the United States, Puerto Rico, Guam, American Samoa, the Commonwealth of the Northern Mariana Islands, or the U.S. Virgin Islands. Report income from this employment on either Short or Long Schedule SE, line 2. If you performed services elsewhere as an employee of a foreign government or an international organization, those earnings are exempt from SE tax.

Exception—Dual citizens. A person with dual U.S.-foreign citizenship is generally considered to be a U.S. citizen for social security purposes. However, if you are a U.S. citizen and also a citizen of a country with which the United States has a bilateral social security agreement, other than Canada or Italy, your work for the government of that foreign country is always exempt from U.S. social security taxes. For further information about these agreements, see the exception shown in the next section.

U.S. Citizens or Resident Aliens Living Outside the United States
If you are a self-employed U.S. citizen or resident alien living outside the United States, in most cases you must pay SE tax. You cannot reduce your foreign earnings from self-employment by your foreign earned income exclusion.

Exception. The United States has social security agreements with many countries to eliminate dual taxes under two social security systems. Under these agreements, you must generally pay social security and Medicare taxes to only the country you live in.

The United States now has social security agreements with the following countries: Australia, Austria, Belgium, Canada, Chile, Czech Republic, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, the Netherlands, Norway, Poland, Portugal, South Korea, Spain, Sweden, Switzerland, and the United Kingdom. Additional agreements are expected in the future.

If you have questions about international social security agreements, you can:

1. Visit the Social Security Administration’s (SSA’s) International Programs website at www.socialsecurity.gov/international;
2. Call the SSA’s Office of International Programs at:
   a. (410) 965-3322 for questions on benefits under agreements, or
   b. (410) 965-7306 for questions on the coverage rules of the agreements; or
3. Write to:
   a. Social Security Administration, Office of International Programs, P.O. Box 17741, Baltimore, MD 21235-7741 USA for information about an agreement, or
   b. Social Security Administration, OIO—Totalization, P.O. Box 17769, Baltimore, MD 21235-7769 USA for information about a claim for benefits.

If your self-employment income is exempt from SE tax, you should get a statement from the appropriate agency of the foreign country verifying that your self-employment income is subject to social security coverage in that country. If the foreign country will not issue the statement, contact the SSA at the address shown in (3a) above. Do not complete Schedule SE. Instead, attach a copy of the statement to Form 1040 and enter “Exempt, see attached statement” on Form 1040, line 56.

Nonresident Alien
If you are a self-employed nonresident alien living in the United States, you must pay SE tax if an international social security agreement in effect determines that you are covered under the U.S. social security system. See Exception under U.S. Citizens or Resident Aliens Living Outside the United States, earlier, for information about international social security agreements. If your self-employment income is subject to SE tax, complete Schedule SE and file it with your Form 1040NR.

Chapter 11 Bankruptcy Cases
While you are a debtor in a chapter 11 bankruptcy case, your net profit or loss from self-employment (for example, from Schedule C or Schedule F) will not be included in your Form 1040 income. Instead, it will be included on the income tax return (Form 1041) of the bankruptcy estate. However, you (not the bankruptcy estate) are responsible for paying SE tax on your net earnings from self-employment.

Enter on the dotted line to the left of Schedule SE, line 3, “Chap. 11 bankruptcy income” and the amount of your net profit or (loss). Combine that amount with the total of lines 1a, 1b, and 2 (if any) and enter the result on line 3.

For other reporting requirements, see Chapter 11 Bankruptcy Cases in the instructions for Form 1040.

More Than One Business
If you had two or more businesses, your net earnings from self-employment are the combined net earnings from all of your businesses. If you had a loss in one business, it reduces the income from another. Figure the combined SE tax on one Schedule SE.

Joint Returns
Show the name of the spouse with self-employment income on Schedule SE. If both spouses have self-employment income, each must file a separate Schedule SE. However, if one spouse qualifies to use Short Schedule SE (front of form) and the other must use Long Schedule SE (back of form), both can use the same form. One spouse should complete the front and the other the back.

Include the total profits or losses from all businesses on Form 1040. Enter the combined SE tax on Form 1040, line 56.

Community Income
The following rules only apply to persons married for federal tax purposes. Registered domestic partners and same-sex spouses in California report community income for self-employment tax purposes the same way they do for income tax purposes. For more information, see Pub. 555.

If any of the income from a business (including farming) is community income, then the income and deductions are reported based on the following:

- If only one spouse participates in the business, all of the income from that business is the self-employment earnings of the spouse who carried on the business.
- If both spouses participate, the income and deductions are allocated to the spouses based on their distributive shares.
- If either or both you and your spouse are partners in a partnership, see Partnership Income or Loss, later.
- If you and your spouse elected to treat the business as a qualifying joint venture, see Qualified Joint Ventures, later.

Married filing separately. If you and your spouse had community income and filed separate returns, attach Schedule SE to the return of the spouse with the self-employment income. Also, attach Schedule(s) C, C-EZ, or F (showing the spouse’s share of community income and expenses) to the return of each spouse.

If you are the spouse who carried on the business, you must include on Schedule SE, line 3, the net profit or (loss) reported on the other spouse’s Schedule C, C-EZ, or F (except in those cases described later under Income and Losses Not Included in Net Earnings From Self-Employment). Enter on the dotted line to the left of Schedule SE, line 3, “Community income taxed to spouse” and the amount of any net profit or (loss) allocated to your spouse as community income. Combine that amount with the total of lines 1a, 1b, and 2 and enter the result on line 3.
If you are not the spouse who carried on the business and you had no other income subject to SE tax, enter “Exempt community income” on Form 1040, line 56, or Form 1040NR, line 54. Do not file Schedule SE. However, if you had $400 or more of other net earnings subject to SE tax, include on Schedule SE, line 1a or 2, the net profit or (loss) from Schedule(s) C, C-EZ, or F allocated to you as community income. Also, enter on the dotted line to the left of Schedule SE, line 3, “Exempt community income” and the allocated amount. If that amount is a net profit, subtract it from the total of lines 1a, 1b, and 2, and enter the result on line 3. If that amount is a loss, treat it as a positive amount, add it to the total of lines 1a, 1b, and 2, and enter the result on line 3.

Community income included on Schedule(s) C, C-EZ, or F must be divided for income tax purposes based on the community property laws of your state. See Pub. 555 for more information.

Qualified Joint Ventures
If you and your spouse materially participate (see Material participation in the 2011 Instructions for Schedule C) as the only members of a jointly owned and operated business, and you file a joint return for the tax year, you can make a joint election to be taxed as a qualified joint venture instead of a partnership.

To make this election, you must divide all items of income, gain, loss, deduction, and credit attributable to the business between you and your spouse in accordance with your respective interests in the venture. Each of you must file a separate Schedule C, C-EZ, or F. On each line of your separate Schedule C, C-EZ, or F, you must enter your share of the applicable income, deduction, or loss. Each of you also must file a separate Schedule SE to pay SE tax, as applicable.

For more information on qualified joint ventures, go to IRS.gov. Enter “qualified joint venture” in the search box and select “Election for Husband and Wife Unincorporated Businesses.”

Rental real estate business. If you and your spouse make the election for your rental real estate business, the income generally is not subject to SE tax. To indicate that election, be sure to check the “QJV” box in Part I, line 2, of each Schedule E that the rental property is listed on. Do not file Schedule SE unless you have other income subject to SE tax. For an exception to this income not being subject to SE tax, see item 3 under Other Income and Losses Included in Net Earnings From Self-Employment, later.

If the election is made for a farm rental business that is not included in self-employment, file two Forms 4835, Farm Rental Income and Expenses.

Fiscal Year Filers
If your tax year is a fiscal year, use the tax rate and earnings base that apply at the time the fiscal year begins. Do not prorate the tax or earnings base for a fiscal year that overlaps the date of a rate or earnings base change.

Line Instructions
Read the flowchart on page 1 of Schedule SE to see if you can use Section A—Short Schedule SE, or if you must use Section B—Long Schedule SE. For either section, you will need to know what your net earnings from self-employment are. To find out what is included as net earnings from self-employment, see Net Earnings From Self-Employment.

TIP Enter all negative amounts in parentheses.

You Have Only Church Employee Income Subject to SE Tax
If your only income subject to SE tax is church employee income (described earlier under Employees of Churches and Church Organizations), also complete lines 5a and 5b. Complete the rest of Schedule SE, as appropriate.

Net Earnings From Self-Employment
In most cases, net earnings include your net profit from a farm or nonfarm business.

Partnership Income or Loss
If you were a general or limited partner in a partnership, include on line 1a or line 2, whichever applies, the amount of net earnings from self-employment from Schedule K-1 (Form 1065), box 14, code A, and Schedule K-1 (Form 1065-B), box 9, code J1. General partners should reduce this amount by certain expenses before entering it on Schedule SE. See your Schedule K-1 instructions. If you reduce the amount you enter on Schedule SE, you must attach an explanation. Limited partners include only guaranteed payments for services actually rendered to or on behalf of the partnership.

If a partner died and the partnership continued, include in self-employment income the deceased’s distributive share of the partnership’s ordinary income or loss through the end of the month in which he or she died. See section 1402(f).

If you were married and both you and your spouse were partners in a partnership, each of you must report your net earnings from self-employment from the partnership. Each of you must file a separate Schedule SE and report the partnership income or loss on Schedule E (Form 1040), Part II, for income tax purposes. If only one of you was a partner in a partnership, the spouse who was the partner must report his or her net earnings from self-employment from the partnership.

Community income. Your own distributive share of partnership income is included in figuring your net earnings from self-employment. Unlike the division of that income between spouses for figuring income tax, no part of your share can be included in figuring your spouse’s net earnings from self-employment.

Registered domestic partners and same-sex spouses in California report community income for self-employment tax purposes the same way they do for income
tax purposes. For more information, see Pub. 555.

Share Farming
You are considered self-employed if you produced crops or livestock on someone else’s land for a share of the crops or live-
stock produced (or a share of the proceeds from the sale of them). This applies even if you paid another person (an agent) to do the
actual work or management for you. Report your net earnings for income tax purposes on Schedule F (Form 1040) and for SE tax
purposes on Schedule SE. See Pub. 225 for details.

Other Income and Losses
Included in Net Earnings
From Self-Employment

1. Rental income from a farm if, as land-
lord, you materially participated in the pro-
duction or management of the production
of farm products on this land. This income
is farm earnings. To determine whether you
materially participated in farm manage-
ment or production, do not consider the ac-
tivities of any agent who acted for you. The
material participation tests for landlords are
explained in chapter 12 of Pub. 225.

2. Cash or a payment-in-kind from the
Department of Agriculture for participating
in a land diversion program.

3. Payments for the use of rooms or
other space when you also provided sub-
stantial services for the convenience of
your tenants. Examples are hotel rooms,
boarding houses, tourist camps or homes,
trailer parks, parking lots, warehouses, and
storage garages. See chapter 5 of Pub. 334
for more information.

4. Income from the retail sale of news-
papers and magazines if you were age 18 or
older and kept the profits.

5. Income you receive as a direct seller.
Newspaper carriers or distributors of any
age are direct sellers if certain conditions
apply. See chapter 5 of Pub. 334 for details.

6. Amounts received by current or for-
mer self-employed insurance agents and
salespersons that are:
   a. Paid after retirement but figured as a
      percentage of commissions received from
      the paying company before retirement,
   b. Renewal commissions, or
   c. Deferred commissions paid after re-
      tirement for sales made before retirement.

However, certain termination payments re-
ceived by former insurance salespersons
are not included in net earnings from self-employment (as explained in item 10
under Income and Losses Not Included in
Net Earnings From Self-Employment).

7. Income of certain crew members of
fishing vessels with crews of normally
fewer than 10 people. See chapter 10 of
Pub. 334 for details.

8. Fees as a state or local government
employee if you were paid only on a fee
basis and the job was not covered under a
federal-state social security coverage
agreement.

9. Interest received in the course of any
trade or business, such as interest on notes
or accounts receivable.

10. Fees and other payments received by
you for services as a director of a corpora-
tion.

11. Recapture amounts under sections
179 and 280F that you included in gross
income because the business use of the
property dropped to 50% or less. Do not
include amounts you recaptured on the dis-
position of property. See Form 4797.

12. Fees you received as a professional
fiduciary. This may also apply to fees paid
to you as a nonprofessional fiduciary if the
fees relate to active participation in the op-
eration of the estate’s business, or the man-
agement of an estate that required extensive
management activities over a long period
of time.

13. Gain or loss from section 1256 con-
tracts or related property by an options or
commodities dealer in the normal course of
dealing in or trading section 1256 con-
tracts.

Income and Losses Not
Included in Net Earnings
From Self-Employment

1. Salaries, fees, etc., subject to social
security or Medicare tax that you received
for performing services as an employee, in-
cluding services performed as an employee
under the railroad retirement system. This
includes services performed as a public of-
ficial (except as a fee basis government em-
ployee as explained in item 8 under Other
Income and Losses Included in Net Earn-
ings From Self-Employment, earlier.

2. Fees received for services performed
as a notary public. If you had no other in-
come subject to SE tax, enter “Ex-
empt—Notary” on Form 1040, line 56. Do
not file Schedule SE. However, if you had
other net earnings of $400 or more subject
to SE tax, enter “Exempt—Notary” and
the amount of your net profit as a notary
public from Schedule C or Schedule C-EZ
on the dotted line to the left of Schedule
SE, line 3. Subtract that amount from the
total of lines 1a, 1b, and 2, and enter the
result on line 3.

3. Income you received as a retired part-
tner under a written partnership plan that
provides for lifelong periodic retirement
payments if you had no other interest in the
partnership and did not perform services
for it during the year.

4. Income from real estate rentals if you
did not receive the income in the course of
a trade or business as a real estate dealer.
Report this income on Schedule E.

5. Income from farm rentals (including
rentals paid in crop shares) if, as landlord,
you did not materially participate in the
production or management of the produc-
tion of farm products on the land. See chap-
ter 12 of Pub. 225 for details. Report this
income on Form 4835. Use two Forms
4835 if you and your spouse made an elec-
tion to be taxed as a qualified joint venture.

6. Payments you receive from the Con-
servation Reserve Program if you are re-
ceiving social security benefits for retire-
ment or disability. Deduct these pay-
ments on line 1b of Schedule SE.

7. Dividends on shares of stock and in-
terest on bonds, notes, etc., if you did not
receive the income in the course of your
trade or business as a dealer in stocks or
securities.

8. Gain or loss from:
   a. The sale or exchange of a capital as-
set;
   b. The sale, exchange, involuntary con-
version, or other disposition of property un-
less the property is stock in trade or other
property that would be includible in inven-
tory, or held primarily for sale to customers
in the ordinary course of the business;
   c. Certain transactions in timber, coal,
or domestic iron ore.

9. Net operating losses from other years.

10. Termination payments you received
as a former insurance salesperson if all of
the following conditions are met.

a. The payment was received from an
insurance company because of services you
performed as an insurance salesperson for
the company.

b. The payment was received after ter-
mination of your agreement to perform
services for the company.

c. You did not perform any services for
the company after termination and before
the end of the year in which you received
the payment.

d. You entered into a covenant not to
compete against the company for at least a
1-year period beginning on the date of ter-
novation.

e. The amount of the payment depended
primarily on policies sold by or credited to
your account during the last year of the
agreement, or the extent to which those pol-
cies remain in force for some period after
termination, or both.

f. The amount of the payment did not
depend to any extent on length of service or
overall earnings from services performed
for the company (regardless of whether eli-
gibility for the payment depended on length
of service).

Statutory Employee Income

If you were a statutory employee, do not
include the net profit or (loss) from Sched-
ule C, line 31 (or the net profit from Sched-
ule C-EZ, line 3), on Short or Long
Schedule SE, line 2. But if you file Long
Schedule SE, be sure to include statutory
employee social security wages and tips from Form W-2 on line 8a.

Optional Methods

How Can the Optional Methods Help You

Social security coverage. The optional methods may give you credit toward your social security coverage even though you have a loss or a small amount of income from self-employment.

Earned income credit (EIC). Using the optional methods may qualify you to claim the EIC or give you a larger credit if your net earnings from self-employment (determined without using the optional methods) are less than $4,480. Figure the EIC with and without using the optional methods to see if the optional methods will benefit you.

Additional child tax credit. Using the optional methods may qualify you to claim the additional child tax credit or give you a larger credit if your net earnings from self-employment (determined without using the optional methods) are less than $4,480. Figure the additional child tax credit with and without using the optional methods to see if the optional methods will benefit you.

Child and dependent care credit. The optional methods may help you qualify for this credit or give you a larger credit if your net earnings from self-employment (determined without using the optional methods) are less than $4,480. Figure this credit with and without using the optional methods to see if the optional methods will benefit you.

Self-employed health insurance deduction. The optional methods of computing net earnings from self-employment may be used to figure your self-employed health insurance deduction.

Using the optional methods may give you the benefits described above, but they may also increase your SE tax.

Changing Your Method

You can change the method after you file your return. That is, you can change from the regular to the optional method or from the optional to the regular method. To do this, file Form 1040X.

Farm Optional Method

You may use this method to figure your net earnings from farm self-employment if your gross farm income was $6,720 or less or your net farm profits were less than $4,851. Net farm profits are:

- The total of the amounts from Schedule F (Form 1040), line 34, and Schedule K-1 (Form 1065), box 14, code A, minus
- The amount you would have entered on Schedule SE, line 1b, had you not used the optional method.

There is no limit on how many years you can use this method.

Under this method, report in Part II, line 15, two-thirds of your gross farm income, up to $4,480, as your net earnings. This method can increase or decrease your net earnings from farm self-employment even if the farming business had a loss.

For a farm partnership, figure your share of gross income based on the partnership agreement. With guaranteed payments, your share of the partnership’s gross income is your guaranteed payments plus your share of the gross income after it is reduced by all guaranteed payments made by the partnership. If you were a limited partner, include only guaranteed payments for services you actually rendered to or on behalf of the partnership.

Nonfarm Optional Method

You may be able to use this method to figure your net earnings from nonfarm self-employment if your net nonfarm profits were less than $4,851 and also less than 72.189% of your gross nonfarm income. Net nonfarm profits are the total of the amounts from:

- Schedule C (Form 1040), line 31,
- Schedule C-EZ (Form 1040), line 3,
- Schedule K-1 (Form 1065), box 14, code A (from other than farm partnerships), and
- Schedule K-1 (Form 1065-B), box 9, code J1.

To use this method, you also must be regularly self-employed. You meet this requirement if your actual net earnings from self-employment were $400 or more in 2 of the 3 years preceding the year you use the nonfarm optional method. The net earnings of $400 or more could be from either farm or nonfarm earnings or both. The net earnings include your distributive share of partnership income or loss subject to SE tax.

Use of the nonfarm optional method from nonfarm self-employment is limited to 5 years. The 5 years do not have to be consecutive.

Under this method, report in Part II, line 17, two-thirds of your gross nonfarm income, up to the amount on line 16, as your net earnings. But you cannot report less than your actual net earnings from nonfarm self-employment.

Figure your share of gross income from a nonfarm partnership in the same manner as a farm partnership. See Farm Optional Method for details.

Using Both Optional Methods

If you can use both methods, you can report less than your total actual net earnings from farm and nonfarm self-employment, but you cannot report less than your actual net earnings from nonfarm self-employment alone.

If you use both methods to figure net earnings, you cannot report more than $4,480 of net earnings from self-employment.