



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF THE CHIEF COUNSEL

November 22, 2016

Number: **2016-0083**
Release Date: 12/30/2016

CONEX-135969-16

UIL: 1402.01-00

The Honorable Marco Rubio
201 South Orange Avenue, Suite 350
Orlando, FL 32801

Attention:

Dear Senator Rubio:

I am responding to your inquiry dated November 2, 2016, on behalf of your constituent, . She asked about the taxation of post-retirement payments she received from and was particularly concerned with whether these payments are subject to self-employment tax.

Under current law, the post-retirement payments she receives from are subject to self-employment tax because the payments resulted from her services on behalf of the company.

The analysis of current applicable law begins with section 1402(b) of the Internal Revenue Code ("the Code"), which states that payments are subject to self-employment tax if they are "net earnings from self-employment derived by an individual . . . during any taxable year." The net earnings this definition refers to are "the gross income derived by an individual from any trade or business carried on by such individual."

Interpreting this provision of the Code, a number of courts—including the United States Tax Court in a case titled *Newberry v. Commissioner*, 76 T.C. 441 (1981)—have concluded that self-employment tax applies when there is "a nexus between the income received and a trade or business that is, or was, actually carried on." The Tax Court in *Newberry* indicated that the income "must arise from some actual (whether present, past, or future) income-producing activity of the taxpayer before such income becomes subject to . . . self-employment taxes."

A Federal Court of Appeals considered the application of this general principle to payments such as those _____ received just this past May. The United States Court of Appeals for the Eleventh Circuit, in a case titled *Peterson v. Commissioner*, 827 F.3d 968 (11th Cir. 2016), addressed whether Mary Kay retirement payments are subject to self-employment tax. The taxpayer in the case was a long-serving Mary Kay National Sales Director who retired from Mary Kay and began receiving post-retirement payments. The court concluded these payments were subject to self-employment tax because they resulted from her association with Mary Kay.

Finally, as _____ correctly observed, section 1402(k) provides that certain payments are not subject to self-employment tax. This exclusion, however, is a narrow one, applying only to certain payments made to former insurance company salesmen (and even then, only if those payments meet a series of specific requirements). Section 1402(k) therefore does encompass the payments she receives from _____. Any broadening of the scope of this provision would require amending the Code. In fact, the request from _____ that you forwarded to us included an attachment that indicated “We are asking for legislation to add [an exemption similar to that provided in section 1402(k)] to Internal Revenue Code Section 1402, to exempt retired _____ from self-employment tax on their post-retirement payments.” We concur that such a change would require legislation.

I am sorry my response is not favorable, but I hope this information is helpful. If you would like to discuss this further, please contact me at _____, or _____ or _____ of my staff, at _____.

Sincerely,

Victoria A. Judson
Associate Chief Counsel
(Tax Exempt & Government Entities)