

TAX COURT REMINDER: PUERTO RICANS ARE SUBJECT TO U.S. SELF-EMPLOYMENT TAX

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By: Mitchell W. Goldberg

In a recent Tax Court decision, *Curet v. Commissioner*, TC Memo 2016-138, the Tax Court reminded us that, although a bona fide resident of Puerto Rico (i.e., an individual who spends a requisite number of days physically present in Puerto Rico and, under the totality of circumstances, generally lives his or her life in Puerto Rico) is generally not subject to U.S. income tax on income sourced in Puerto Rico, such resident is still subject to U.S. self-employment taxes on his or her net earnings from self-employment. Under Internal Revenue Code (the "Code") § 933, a bona fide resident of Puerto Rico is not subject to U.S. income tax on income sourced to Puerto Rico (under the sourcing rules of the Code), other than income received as compensation for services rendered as an employee of the United States or any agency thereof. The Code generally sources compensation for personal services rendered to the jurisdiction where the services were performed. As such, unless a bona fide resident of Puerto Rico is an employee of the United States or one of its agencies, compensation for personal services rendered in Puerto Rico is not subject to U.S. income taxes. However, the Code § 1402(a)(6) requires a resident of Puerto Rico to compute his or her net earnings from self-employment in the same manner as a U.S. citizen without regard to Code § 933. A Puerto Rican resident, who is not otherwise required to file a Form 1040, reports net earnings from self-employment on IRS Form 1040-SS or may file a Form 1040-PR in lieu of a 1040-SS.

In *Curet*, an individual taxpayer who lived in Puerto Rico for the entire taxable year (whether he was a bona fide resident was not at issue) received income for consulting services rendered in Puerto Rico. Such income exceeded his related expenses, resulting in net income from self-employment for the taxpayer. The taxpayer did not file any return with the U.S. reporting his net earnings from self-employment and paid no self-employment taxes. The Commissioner assessed a deficiency against the taxpayer for unpaid self-employment taxes on his consulting income. The taxpayer in *Curet*, appearing pro se (i.e., without an attorney), argued that, because he was a bona fide resident of Puerto Rico, none of his income was subject to any U.S. tax. The Tax Court rejected the taxpayer's argument and held for the Commissioner.

In short, the Code imposes self-employment taxes on a Puerto Rican resident's net earnings from self-employment, regardless of whether the income which gave rise to such earnings is excluded from U.S. income taxes under Code § 933.

If you have any questions on this topic, please contact the author, [Mitchell W. Goldberg](#), on the firm's [Business, Finance & Tax Team](#).

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