INCOME

EARNED INCOME

D. SELF-EMPLOYMENT

Net Earnings from Self-employment (NESE) is the gross income from any trade or business less allowable deductions for that trade or business. NESE also includes any profit or loss in a partnership.

1. Determining Monthly NESE

Divide the entire taxable year's NESE equally among the number of months in the taxable year, even if the business:

- is seasonal;
- starts during the year;
- ceases operation before the end of the taxable year; or
- ceases operation prior to initial application for SSI.

2. Offsetting Net Loss

Divide any **verified** net loss for a taxable year evenly over the months in the taxable year. Subtract each resulting monthly amount from the individual's or couple's other earnings in the same month. Apply this procedure whether a couple filed a joint income tax return or separate returns, and regardless of which member of the couples listed below incurred the loss:

- an eligible couple;
- an eligible individual with an ineligible spouse;
- two parents;
- a sponsor and his/her spouse

3. Work Expenses

If an individual is self-employed (whether or not he/she is also a wage earner), reduce his/her earned income by any allowable work expenses which have not already been used to compute NESE.

INCOME

EARNED INCOME

4. Deduction for Taxable Years After 1989

For taxable years beginning after 1989, a 7.65 percent deduction is applied to net profit in determining NESE. Therefore, net profit is multiplied by .9235 to determine NESE. Refer to "How to Verify NESE" to find the correct NESE amount on the Federal income tax forms.

NOTE: This deduction recognizes, as a business expense, part of the Social Security taxes paid. If Social Security tax is not paid (e.g., in situations involving less than $400 per year in NESE, net losses, and when no tax return is filed), the deduction does not apply.

5. Withdrawals for Personal Use

When an individual alleges (or the worker discovers) cash or in-kind items are withdrawn from a business for personal use, proceed as follows:

Ask the individual whether the withdrawals were **properly accounted for** in determining NESE. That is, were they either deducted on the individual's Federal income tax return in determining the cost of goods sold or the cost of expenses incurred, or deducted on his business record.

IF THE WITHDRAWALS ARE...	THEN...
Properly accounted for	Do not charge them again as income.

INCOME

EARNED INCOME

IF THE WITHDRAWALS ARE...	THEN...
Not properly accounted for	- Ask the individual to estimate the value of the cash or in-kind withdrawals. Deduct that amount from the cost of goods sold or the cost of expenses incurred on the profit and loss statement to arrive at the proper NESE.
Not properly accounted for	If the individual cannot or will not provide the profit and loss statement, but alleges an amount of NESE, add the value of the withdrawals to the individuals allegation of NESE.

6. How to Verify NESE

Verify NESE whenever an individual is self-employed or has been self-employed during the current taxable year. Verify NESE by obtaining the most recent federal income tax return filed with IRS. If the business is new, use the individual's business records or the best estimate available.

The Federal income tax return contains evidence of NESE in the following schedules:

a. Schedule SE

- Net earnings - Section A, line 4 or Section B, line 4.C. **NOTE:** If line 4 or 4C shows a positive amount of less than $400, then line 3 is used, even if the amount on line 3 is greater than $400. For example, line 3 shows $410 and line 4/4C shows $378. Line 3 should be used because no tax was due.

- Net loss - Section A, line 3 or Section B, line 4.C.

b. Schedule C - Line entitled "Net Profit or Loss."

c. Schedule F - Line entitled "Net Profit or Loss."

7. How To Estimate NESE for Current Taxable Year

Use the first of the following procedures which is applicable. Document the file so that it supports the estimate made by the worker.

WHEN TO USE	METHOD
When an individual:	Current Year's Estimate Based on Prior Year's Profit
- has been conducting the same trade or business for several years;	Use the NESE from the prior year as an estimate for the current taxable year.
- has had NESE which has been fairly constant from year-to-year; and	
- anticipates no change or gives no satisfactory explanation of why current NESE would be substantially lower than past NESE	

INCOME

EARNED INCOME

When an individual:	Gross-Net Ratio
- is engaged in the same business that he/she had **only** in the preceding taxable year; and	- Calculate from the individual's tax return or business records the ratio between net profit and gross receipts for the last year. **EXAMPLE:** Net profit of $1,200 for $6,000 gross income or 20 percent.

When an individual:	Gross-Net Ratio
- anticipates no change or gives no satisfactory explanation of why current NESE would be substantially different from what it has been in the past	- Calculate from his/her records the actual gross receipts for the current taxable year and project it for the remainder of the year. **EXAMPLE: $4,000** in current year's receipts for the first 6 months gives an assumed gross of $8,000 for the entire year. - Apply the previously calculated gross-net ratio to the current year's assumed gross to arrive at the estimated NESE. **EXAMPLE:** 20 percent of $8,000 is $1,600.

INCOME

EARNED INCOME

EXCEPTION: Do not use this method for businesses which are seasonal or have unusual income peaks at certain times of the year; go to next applicable procedure.

When an individual is engaged in a new business

Projecting Partial Year's Profit for Whole Year

- Obtain the individual's profit and loss statement or other business records for his/her taxable year to date.

When an individual is engaged in a new business

Projecting Partial Year's Profit for Whole Year

- Ascertain his/her net profit to date.

- Project that net profit for the entire taxable year.

EXCEPTION: Do not use this method for businesses which are seasonal, or have unusual income peaks at certain times of the year; go to next applicable procedure.

INCOME

EARNED INCOME

When: - an individual is engaged in a new business and records are not yet available; or - the business has been going on for some time but no records were kept	Individual's Estimate Use a signed allegation of the individual's best estimate.
When an individual: - alleges his/her NESE for the current year will vary from for past years; and - gives a satisfactory explanation for the variation	**Current Year's Estimate Varies from Past Records** - Obtain a written statement from the individual explaining the basis for the NESE variation. - If the individual's estimate of NESE for the current year is higher than that of the prior years, and the individual satisfactorily explains why, accept the individual's estimate of NESE. **EXAMPLE:** Individual recently added new products to his mail order sales catalog and sales have picked up dramatically.

INCOME

EARNED INCOME

- If the individual's estimate of NESE for the current year is lower than that of prior years, and the individual satisfactorily explains why, request any relevant documentation for the file and accept the lower estimate.

EXAMPLES:

- Satisfactory Explanation - the business has suffered a heavy loss or damage due to fire, flood, burglary, serious illness or disability of the owner, or other catastrophic event.

- Relevant Documentation - copies of newspaper accounts of the event, police reports, etc.

NOTE: In some cases (e.g., downturns in the economy) there may not be any documentation of the event. In such cases, the individual's written statement explaining the basis for the variation is sufficient documentation.