



Sirius Solutions, L.L.L.P. v. Commissioner: The Fifth Circuit’s Decision Interpreting the Limited Partner Exception to Self- Employment Taxes

April 30, 2026

On January 16, 2026, in *Sirius Solutions, L.L.L.P. v. Commissioner*, a divided three-judge panel for the U.S. Court of Appeals for the Fifth Circuit (Fifth Circuit) [rejected](#) the Tax Court’s interpretation of the limited partner exception to self-employment taxes. Under Internal Revenue Code (IRC) § [1402\(a\)\(13\)](#), taxpayers who are “limited partners” can qualify to exclude their distributive share of partnership income (or loss) from self-employment income. The term “limited partner” for purposes of the limited partner exception is [not defined](#) in the IRC. As a result, there are multiple [cases](#) discussing the application of self-employment taxes to partners that [turn on](#) the meaning of *limited partner*.

In *Sirius Solutions*, the Fifth Circuit majority [interpreted](#) *limited partner* for purposes of the limited partner exception to mean “a partner in a limited partnership that has limited liability” and rejected the Tax Court’s functional analysis and “passive investor” interpretation. The [Fifth Circuit](#) vacated the Tax Court’s ruling and sent the case back to the Tax Court for “further proceedings consistent” with its limited liability interpretation. As a consequence, state-law limited partners who have limited liability under state law and are acting in a partner capacity might not be subject to federal self-employment taxes even when they actively participate in limited partnership business.

On April 1, 2026, the government [petitioned](#) the Fifth Circuit for a [rehearing en banc](#) in *Sirius Solutions*. Challenges to the Tax Court’s functional analysis and *limited partner* interpretation are pending before the U.S. Courts of Appeals for the [First](#) and [Second](#) Circuits.

Past attempts by the Department of the Treasury (Treasury) and the Internal Revenue Service (IRS) to restrict eligibility for the limited partner exception have been [unsuccessful](#).

This Legal Sidebar provides an overview of how self-employment taxes and Social Security benefits apply to limited partners, summarizes the Fifth Circuit’s decision in *Sirius Solutions*, and discusses considerations for Congress.

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Self-Employment Taxes and Social Security Benefits

In general, self-employed individuals must pay [Social Security taxes](#) and [Medicare taxes](#) funding Medicare Part A or Hospital Insurance (collectively, Self-Employed Contributions Act [SECA] taxes). These self-employment taxes are [determined](#) using an individual's "self-employment income," which is [defined](#) in IRC § 1402(b) as "net earnings from self-employment." The Social Security tax rate is [12.4%](#) on self-employment income up to an [annual limit adjusted by average wage growth](#) ([\\$184,500 in 2026](#)). The Medicare tax rate is [2.9%](#) on all self-employment income. A [0.9%](#) additional Medicare tax applies to self-employment income above thresholds that vary based on filing status (i.e., \$250,000 for joint returns; \$125,000 for married filing separately; and \$200,000 for others). As part of the Social Security Amendments of 1977 (P.L. 95-216), Congress [amended](#) IRC § 1402(a) to exclude a limited partner's partnership share of income or loss from Social Security and Medicare taxes, subject to exceptions. In the same section of the Social Security Amendments of 1977, Congress [amended](#) Section 211 of the Social Security Act to exclude a limited partner's partnership share of income or loss from net earnings from self-employment for Social Security purposes.

IRC § 1402 contains special rules applicable to [partners in a partnership](#) when calculating their self-employment tax liability. Under IRC § [1402\(a\)](#), net earnings from self-employment expressly *includes* a partner's "distributive share (whether or not distributed) of income or loss described in section [702\(a\)\(8\)](#) from any trade or business carried on by a partnership of which he is a member." IRC § [1402\(a\)\(13\)](#) expressly *excludes* a limited partner's distributive share from net earnings from self-employment. Specifically, IRC § 1402(a)(13) provides an [exclusion](#) for

the distributive share of any item of income or loss of a limited partner, as such, other than guaranteed payments described in section [707\(c\)](#) to that partner for services actually rendered to or on behalf of the partnership to the extent that those payments are established to be in the nature of remuneration for those services.

"Guaranteed payments," as described in IRC § [707\(c\)](#), [are](#) "payments to a partner for services or the use of capital" that are paid without regard to partnership income. Because of the guaranteed payment for services carveout in IRC § [1402\(a\)\(13\)](#), a limited partner can have self-employment income subject to self-employment taxes when a limited partner receives a guaranteed payment for services rendered to the partnership and that payment is in the nature of remuneration for services.

Additionally, the amount of Social Security benefits an individual receives [depends, in part](#), on an individual's [net earnings from self-employment](#). Parallel to IRC § [1402\(a\)\(13\)](#), under Section 211(a)(12) of the Social Security Act, net earnings from self-employment are similarly [excluded from a limited partner's distributive share](#).

[Pursuant to these sections](#), when a limited partner's distributive share of partnership income is not subject to SECA taxes, that income [typically](#) does not count toward Social Security benefits.

Sirius Solutions

Case History

Before the Fifth Circuit's 2-1 decision in *Sirius Solutions*, in multiple [cases](#), the Tax Court [employed](#) a functional analysis to determine when a limited partner under state law was a limited partner under IRC § [1402\(a\)\(13\)](#). In 2023, in *Soroban Capital Partners LP v. Commissioner*, the Tax Court [determined](#) that Congress intended the limited partner exception to apply to state-law limited partners who were "passive investors" and held that a functional analysis test should be used to decide whether the limited partner exception applied. In 2024, when the matter in *Sirius Solutions* was before the Tax Court, the Tax

Court explained that *stare decisis* principles obligated it to follow its limited partner interpretation in *Soroban*. In response, Sirius Solutions requested, and the Tax Court granted, a decision for the government, so that Sirius Solutions could challenge the Tax Court's holding in *Soroban* in the Fifth Circuit.

Facts

Sirius Solutions, L.L.P., a limited liability limited partnership formed in Delaware and based in Texas, **operated** a business consulting firm. In the 2014-2016 tax years, the firm **was owned** by several individual limited partners and one general partner—a limited liability company (LLC). The LLC general partner's **interest** in the limited partnership was less than 1%. On the firm's 2014, 2015, and 2016 tax returns, the firm **allocated** all of its ordinary business income to its limited partners. The firm "**reported** ordinary business income of \$5,829,402 in 2014, \$7,242,984 in 2015, and -\$490,291 in 2016." Pursuant to the limited partner exception in IRC § 1402(a)(13), the firm "**did not** report any net earnings from self-employment to any of the individual partners." The **IRS** audited the firm's returns and adjusted the firm's net earnings from self-employment—an increase of \$5,915,918 for 2014; an increase of \$7,372,756 for 2015; and a decrease of \$490,291 for 2016.

Opinion

Applying the Supreme Court's framework in *Loper Bright Enterprises v. Raimondo* to determine the meaning of a statute, the 2-1 majority **held** that the "single, best meaning" of limited partner in IRC § 1402(a)(13) was "a partner in a limited partnership that has limited liability." The majority **began** its analysis by studying contemporaneous dictionary definitions, then looked to the IRS's long-standing definition in partnership return instructions, and the Social Security Administration's (SSA's) long-standing rule defining *limited partner* for the purpose of Section 211(a)(12) of the Social Security Act. After reviewing multiple dictionaries, the majority **announced** that "limited liability" was the "touchstone" of a "limited partner" at the time of the exception's enactment.

The majority **observed** that the definition of *limited partner* used by the IRS in its partnership return instructions remained consistent for more than 40 years. It explained that the 1978 partnership return instructions **defined** a *limited partner* as "one whose potential personal liability for partnership debts is limited to the amount of money or other property that the partner contributed or is required to contribute to the partnership" and **did not refer** to a "passive investor." Quoting *Loper Bright*, the majority **considered** this particular contemporaneous and consistent agency interpretation "especially useful" in determining the meaning of the phrase "limited partner." In the majority's **view**, the IRS's partnership return instructions definition was even more useful because it provided information "to the public" in an effort to "**help taxpayers comply with the law.**"

Similarly, the majority **found** support for its statutory interpretation in the SSA's long-standing **rule** defining *limited partner* for the purpose of Section 211(a)(12) of the Social Security Act. The majority **explained** that the SSA's interpretation should be given "due respect" in interpreting *limited partner* under IRC § 1402(a)(13) because "[b]oth Social Security taxes and benefits depend on an individual's net earnings from self-employment." The 1980 SSA rule **provided** that a person is a "'limited partner' if [the person's] financial liability for the obligations of the partnership is limited to the amount of [the person's] financial investment in the partnership." In the majority's view, the SSA rule **confirmed** that limited liability was "the touchstone" of the term *limited partner* at the time of the exception's enactment.

The majority **acknowledged and discounted** the latter part of the SSA's long-standing rule, which **provides** that limited partners generally "will not have to perform services." It **reasoned** that the latter part of the rule did not mean a limited partner was prohibited from, "or generally d[id] not[,] perform services for the partnership." The prevailing opinion **determined** that the latter part of the SSA rule did not change the

focus of the *limited partner* definition from the limited liability component. The majority also **concluded** that the latter part of the SSA rule did not support a definition of *limited partner* that only applied to passive investors.

Next, the 2-1 majority **addressed** the Tax Court's, the IRS's, and the dissent's counterarguments. The majority **reasoned** that interpreting the limited partner exception to apply only to "passive investors" was "**wrong**" because the interpretation was undermined by IRC § 1402(a)(13)'s guaranteed payment clause, Congress had shown its ability to write laws addressing "passive" activities, and the interpretation required a functional analysis that produced taxpayer uncertainty. The majority **responded** to arguments that a limited liability interpretation conflicted with federal tax principles—"[f]ederal law, not state law, controls the interpretation of federal tax statutes"; "[f]ederal tax law is concerned with economic reality, not labels"; and "federal tax law should be uniform nationwide." The majority **explained** that it had to look to state law to determine whether the state-controlled preconditions to the federal definition of *limited partner* were met. The majority **expressed** that it looked beyond state labels because it looked to the "substantive 'interests' that state law creates"—whether a taxpayer had "the rights and duties associated with a limited partnership or whether that individual ha[d] limited liability." The prevailing view **determined** that there was "no serious risk" to federal law uniformity as differences in state law did not equate to "disuniformity" and most states had adopted uniform limited partnership acts.

An **analysis** of the Tax Court's textual argument in *Soroban* that the limited partner exception in IRC § 1402(a)(13) only applies to a subset of limited partners is included in the majority's opinion. In *Soroban*, the Tax Court **decided** that Congress's addition of "'as such' . . . made clear that the limited partner exception applies only to a limited partner who is functioning as a limited partner." From there, the Tax Court **looked** to IRC § 1402(a)(13)'s legislative history and "confirmed [its] conclusion" that "Congress enacted section 1402(a)(13) to exclude earnings from a mere investment" and intended the provision "to apply to partners that are passive investors." The 2-1 majority in *Sirius Solutions* did not reach the same conclusion because it **did not construe** "as such" to "restrict or narrow the class of limited partners, []or . . . upset the term's ordinary meaning." To the majority, "as such" was added to "**clarif[y]**" how dual status partners are taxed. It **explained** "[a]t the time the statute was enacted, just as today, an individual could **serve as both** a limited partner and a general partner" and limited partners could have "multiple functions or capacities." As follows, the majority **determined** that when a taxpayer is "functioning as a limited partner, [the] taxpayer's distributive share of partnership income (or loss) is excluded from net earnings from self-employment," "[b]ut when functioning as a general partner, [the taxpayer's] distributive share is included in net earnings from self-employment."

In the majority's view, the history of limited partnership law and the legislative history of IRC § 1402(a)(13) **did not strengthen** the government's case. The majority **found** that state laws on limited partnerships were in "constant flux" and the "only clear rule derivable from that ever-changing patchwork [wa]s . . . a limited partner had limited liability." It **was not** enough that the "Revised Uniform Limited Partnership Act of 1976 [(RULPA)] set some . . . limits on the ability of limited partners to participate in the control of [a] limited partnership," as that did not "change the core of what it *mean[t]* to be a limited partner." The majority **was** reluctant to "probe the legislative history," but did examine House Ways and Means Committee Report 95-702, which was, in the majority's view, the "best evidence" supporting the government's position that the limited partner exception in IRC § 1402(a)(13) only applied to passive investors. The majority **discussed** the language in the House report that revealed the committee's "concern[] about situations in which certain business organizations solicit investments in limited partnerships as a means for an investor to become insured for social security benefits." The majority also **acknowledged** the House report's explanation that "the exclusion from coverage would not extend to guaranteed payments (as described in section 707(c) of the Internal Revenue Code), such as salary and professional fees, received for services actually performed by the limited partner for the partnership." Despite its review of the House report, the majority **dismissed** the government's legislative history argument because the legislative history "sa[id] nothing about *how* Congress sought to fix the

perceived issue.” The majority [determined](#) that the “plain text of the statute d[id] not yield that result” and “[n]either d[id] the House Report.”

Considerations for Congress

Some tax commentators have expressed opinions that the majority’s focus on “limited liability” discounted the [history of uniform limited partnership laws](#) and how those laws initially took into account a limited partner’s partnership activities to determine whether a limited partner retained limited liability and the [history of entity classifications](#). For example, some tax [commentators](#) have observed that over [time](#), uniform laws changed from prohibiting limited partners from participating in partnership business to permitting limited partners to participate in more partnership activities without losing liability protection. It is unclear whether U.S. Courts of Appeals outside the Fifth Circuit might be [receptive to contentions](#) that at the time of IRC § 1402(a)(13)’s enactment state-law limited partners were generally not entitled to limited liability unless they “refrain[ed]” from partnership business.

In the past, Treasury and the IRS have attempted to restrict eligibility for the limited partner exception. In 1997, Treasury [issued](#) a proposed regulation defining *limited partner* for purposes of IRC § 1402(a)(13). Soon after, Congress enacted the Taxpayer Relief Act of 1997 (P.L. 105-34), which [provided](#), “No temporary or final regulation with respect to the definition of a limited partner under section 1402(a)(13) of the Internal Revenue Code of 1986 may be issued or made effective before July 1, 1998.” A “Sense of Senate resolution” might [offer](#) some insight on the reasons for the moratorium: “the proposed regulations address and raise significant policy issues and the proposed definition of a *limited partner* may have a substantial impact on the tax liability of certain individuals and may also affect individuals’ entitlement to social security benefits.” Therefore, the Sense of Senate Resolution [concluded](#) that Treasury and the IRS should withdraw the proposed regulation and “Congress . . . should determine the tax law governing self-employment income for limited partner.”

Because this case turns on a statutory term, Congress could consider passing legislation clarifying the scope of the limited partnership exception to provide a consistent *limited partner* definition for purposes of IRC § 1402(a)(13). For example, to prevent active state-law limited partners with limited liability from circumventing SECA taxes, Congress may adopt statutory text like IRC § 1402(a)(10) or the 1997 proposed regulation. Alternatively, Congress could adopt language that clarifies that limited liability is all that is required to be a *limited partner* under IRC § 1402(a)(13). Congress may also consider clarifying the extent to which partners and members of other state-law entities, such as limited liability partnerships and limited liability companies, are eligible for the limited partner exception. Congress could also leave this matter for resolution in the courts.

In the government’s *Sirius Solutions* petition for rehearing en banc, the government [contends](#) that “heavy losses in tax revenues” would stem from the Fifth Circuit’s 2-1 decision and those losses threaten “critical funding for Social Security and Medicare.” The government [asserts](#), “[t]he IRS estimates that revenue at stake exceeds \$500 million, just in pending matters.” The government claims that these revenue losses [are](#) “expected to grow, as the majority’s approach encourages more businesses to organize as limited partnerships and use distributive shares to compensate workers who already qualify for benefits.” To the extent that Congress seeks to address the government’s claims concerning [Social Security](#) and [Medicare Part A](#) funding, Congress could consider raising the earnings base for [Social Security](#) taxes and the [additional 0.9% Medicare](#) tax and increasing [Social Security](#) and [Medicare](#) tax rates.

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