

S-E-C-R-E-T

Chief of Station, Mexico City

Office of Finance

LIRUFF/1 - 1963 Taxes

HQS-4998, 28 October 1964

1. A review of each of the statements made in reference by LIRUFF/1 has been made by Headquarters. Some of these statements can be used to substantiate a claim that the KUBARK earnings are non-taxable.

2. The fact that an employer-employee relationship does not exist is not a basis for determining whether earnings are taxable. Subject is a contract agent-independent contractor; and the payment received by LIRUFF/1 is considered earned income. The law (Internal Revenue Code) defines earned income as wages, salaries, professional fees, and other amounts received as compensation for personal services actually rendered. Earned income is excludable if the qualifications of Section 911 of the Internal Revenue Code are met. Three of these qualifications are:

- A. Earned income from sources without the U. S.
- B. Attributable to such uninterrupted period-one complete tax year or 510 days out of an 18 month period.
- C. Not paid by the United States or any Agency or instrumentality thereof.

Subject obviously qualifies on (A) and (B), however, LIRUFF/1 does not meet qualification (C), therefore, exclusion cannot be claimed for the income earned from KUBARK.

Attachments:
 1963 Covert Tax Returns
 Sec. of IRS Code (See para. 4)
 Distribution:
 3 - Mexico City/w/attachs.

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- 3 - CTD/CTB
- 2 - Division
- 1 - OF Brg.
- 1 - RI/EP

OF/CTD/CTB Powell/alh
 VE/EP

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C/VE/SS

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3. If Subject read IRS Publication No. 54 (Tax Guide for U. S. Citizens Abroad) it is easily understandable how he could be misled because they refer to Government employees and not to those individuals having an independent contractor relationship with the Government. The key point in the Revenue regulations is the definition of earned income and the fact that earned income is not excludable if earned from a U. S. Government source.

4. Attached are photocopies of the Internal Revenue Code and regulations pertaining to the exclusion of income earned abroad.

5. Also attached is the 1963 covert tax return which Headquarters has prepared. Please note that lines 17 thru 23 and the Schedule C (lines 6-11) have not been completed. If LIHJFF/1'S overt income has maximum social security (FICA) withheld no self-employment (social security) tax is computed. If social security is not withheld overtly then self-employment tax is computed on the Schedule C and added to the income tax on the Form 1040 (see line 17, Form 1040). The Form 1040 can then be completed, signed, and returned to Headquarters along with the payment for the outstanding tax liability.

6. If a personal check is used in payment of the tax liability it should be prepared in accordance with FHB 20-661-1, Supplement, paragraph 9 (see of a ~~different~~ ~~same~~ ~~as~~ ~~the~~ ~~page~~).

DORA B. FERRECKY