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Sirius Solutions, L.L.L.P. v. Commissioner—Impact on SECA Tax for Limited Partners

In a landmark decision released on January 16, 2026, the U.S. Court of Appeals for the Fifth Circuit vacated the Tax Court's ruling in *Sirius Solutions, L.L.L.P. v. Commissioner*. The court held that the "limited partner" exception to self-employment (SECA) taxes depends on a partner's legal status under state law, not on whether they are "passive" or "active" in the business. This ruling creates a significant departure from the Tax Court's prior approach and provides a path for taxpayers in the Fifth Circuit (Texas, Louisiana and Mississippi) to potentially exclude distributive shares of partnership income from self-employment taxes.

Under Internal Revenue Code Section 1402(a)(13), the distributive share of income for a "limited partner, as such" is generally excluded from net earnings from self-employment. For years, the IRS and the U.S. Tax Court (most notably in *Soroban Capital Partners v. Commissioner*) have argued that this exclusion applies only to "passive investors." They utilized a functional analysis test, looking at:

- The partner's level of participation in management.
- The amount of time the partner spent on partnership business.
- Whether the partner had the authority to bind the partnership.

In *Sirius Solutions*, the Tax Court had previously sided with the IRS, ruling that because the partners were active and not passive in the business, they did not qualify for the exemption despite being limited partners under state law.

The Fifth Circuit flatly rejected the Tax Court's approach, focusing instead on the plain text of the statute. The court ruled that a limited partner is simply a partner in a limited partnership whose liability is limited to their investment under state law. The court found no requirement in the plain meaning of the statute that a limited partner must be passive to qualify for the exclusion. The court interpreted the phrase "limited partner, as such" to mean that the partner must receive the income in their capacity as a limited partner, rather than through other payments like guaranteed payments for services (which remain subject to SECA). Notably, the court did not discuss whether members of other common types of state-law legal entities (such as limited partners in state-law LLPs or members of state-law LLCs) may also qualify for the limited partner exception.

This ruling creates a direct conflict with the Tax Court and potentially other circuits (such as the First and Second Circuits, where appeals are pending). This split increases the likelihood that the U.S. Supreme Court eventually will have to resolve the definition of a limited partner.

In summary, *Sirius Solutions* clarifies that, at least in the Fifth Circuit, the SECA exemption for limited partners is determined by state-law status and limited liability, not by the partner's level of activity in the partnership.

This memorandum is to provide an overview of recent case law and its impact. It is for general informational purposes only and should not be considered or relied on as a legal opinion of Kutak Rock. If you have questions, please contact any member of [Kutak Rock's National Tax Practice Group](#). You may also visit us at www.kutakrock.com.

