OFFICE OF
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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR DISTRICT COUNSEL,

Attention:

FROM: Chief, Branch 2
CC: EBEO

SUBJECT: Medical Resident FICA student exception claim request for Field Service Advice

This Field Service Advice responds to your memorandum dated October 20, 1999. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND

University =

State =

State Retirement System =

ISSUES

1. Whether University medical residents' services are covered under the State's § 218 agreement and are therefore subject to FICA.

2. If the medical residents' services are not covered under the State's § 218 agreement, whether the residents' services are excepted from the FICA based upon the student FICA exception.

CONCLUSIONS

1. University medical residents appear not to be covered under the State's § 218 agreement. The facts indicate that University medical residents were not eligible to participate in the State Retirement System and therefore were not members of the State Retirement System coverage group.

2. Because University medical residents appear not to be covered under the State's § 218 agreement, the Service must determine whether the residents' services are excepted from FICA based upon the student FICA exception. We will soon provide guidance to field personnel on the facts to be developed in identifying the entity that is the common law employer and whether a medical resident is a student who is enrolled and regularly attending classes.

FACTS

The University sponsors a graduate medical education (GME) program. The University has agreements with many hospitals to provide the hospitals with medical resident services.[1] In return, the hospitals have agreed to act as teaching hospitals.[2] The University filed a claim for refund of FICA taxes it withheld and paid with respect to remuneration paid to University medical residents during the years through .

In , the State entered into an agreement under § 218 of the Social Security Act (the "Act") with the Social Security Administration (SSA) to cover certain of its employees under social security ("§ 218 agreement"). In , the State modified its § 218 agreement to include as a coverage group members of the State Retirement System. This modification excludes the services of students which would be excluded if performed for a private employer. In , the § 218 agreement was modified to include services performed by University employees in positions covered by the State Retirement System. This modification was made retroactive to .

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[1]This memo refers to all participants in the University GME program as "residents." First year residents are often referred to as "interns." Internship programs were discontinued across the country in 1975, and residency programs, including the University's, have since included medical school graduates in their first year of graduate medical education.

[2]For purposes of this memo, the term "hospital" means any facility that has as its purpose the provision of medical care to patients, including outpatient medical clinics that provide outpatient services.

Between and , medical residents and interns were considered students by the state and thus their positions were not considered eligible for membership in the State Retirement System. Thus, the State did not consider medical residents to be members of the State Retirement System coverage group for § 218 agreement coverage purposes. In , a State law was enacted to provide that

Effective January 1, , the State began paying Medicare tax with respect to medical residents' services. Effective July 1, , the State began paying both the Medicare and OASDI portions of social security with respect to medical residents' services.

LAW AND ANALYSIS

The Student FICA Exception

Sections 3101-3126 of the Internal Revenue Code impose Federal Insurance Contribution Act (FICA) taxes on the wages of employees. FICA taxes consist of an old-age, survivors, and disability insurance portion (OASDI) (usually called social security tax) and a Medicare portion.

Section 3121(b)(10) of the Code excepts from the definition of employment for FICA purposes services performed in the employ of a school, college, or university ("S/C/U") (whether or not that organization is exempt from income tax), or an affiliated organization that satisfies section 509(a)(3) of the Code in relation to the S/C/U ("related § 509(a)(3) organization") if the service is performed by a student who is enrolled and regularly attending classes at that S/C/U. Thus, the student FICA exception applies to services only if both the "employer status" and "student status" requirements are met.

Determining the Common Law Employer

The first step in determining whether a medical resident's services are subject to the FICA is to identify the resident's common law employer. Section 31.3121(b)(10)-2(c) of the Employment Tax Regulations provides that the status of the employee as a student performing the services shall be determined on the basis of the relationship of such employee to the organization for which the services are performed. Thus, the identity of the common law employer is essential to determining whether the exclusion under § 3121(b)(10) applies (because the common law employer must be a S/C/U or a related § 509(a)(3) organization). Identifying the common law employer is also essential to determining whether the resident is covered by a § 218 agreement (discussed below). The University GME

program has agreements with many teaching hospitals to provide the hospitals with medical resident services. The question therefore arises whether the University or the hospital(s) where the services are performed is the resident's common law employer.

The common law employer is the party that has direction and control over the medical resident. Direction and control is the test not just for determining whether the worker is an employee versus independent contractor, but also determines which party is the employer when the worker has a relationship with more than one entity. The field agent should refer to the training materials that the agent should have received on employee versus independent contractor status. "Independent Contractor or Employee?" Training 3320-102 (Rev. 10-96) TPDS 84238I.

The facts developed thus far are insufficient to determine whether the University or the participating hospitals would be the common law employer(s) of the medical residents. The National Office will soon provide guidance to field personnel on the facts to be developed with respect to this question.

Coverage Under the State's Section 218 Agreement

If it is concluded that the University is the common law employer with respect a resident's services, it must determined whether those services are covered by the State's § 218 agreement. When a state enters into a § 218 agreement with the SSA, employees of the state and its political subdivisions are brought under the agreement in groups known as "coverage groups." The Act gives each state the right to decide which coverage groups to include under its § 218 agreement. Coverage groups fall into two categories: employees who are not covered under a state or local retirement system and employees who are covered under a retirement system. For example, one possible coverage group is the employees of each institution of higher education who are covered under the state retirement system.

The services of certain employees who are members of a coverage group may be optionally or mandatorily excluded from coverage under the state's § 218 agreement. Section 218(c) of the Act provides for certain mandatory and optional exclusions (in the case of any coverage group) from coverage under a § 218 agreement. For example, under § 218(c)(5), a state has the option of excluding the services of students. Section 218(c)(5) provides that the optional exclusion will apply only to students who would be excluded under the general student exclusion provided under § 210(a)(10). Section 210(a)(10) provides for a general exclusion from social security coverage for services performed for a S/C/U (or an organization that is a related § 509(a)(3) organization with respect to the S/C/U) by a student

who is enrolled and regularly attending classes at the S/C/U.[3] But if a state chooses not to exclude student services under its agreement, those services will be covered under social security notwithstanding the general student exclusion under § 210(a)(10) of the Act.

Thus, in determining whether an employee is covered under a state's § 218 agreement, the Service must first determine whether the employee is a member of a coverage group that is included under the state's § 218 agreement. If an employee is not a member of a coverage group, the employee is not covered under the § 218 agreement. If the employee is a member of a coverage group, the question then becomes whether the employee's services are excluded under either a mandatory or optional exclusion.

In the instant case, the State has never treated medical residents as eligible to participate in the State Retirement System.

. Whether employees in a particular position are eligible for membership in a state retirement system is generally a question of state law. Thus, it appears that the medical residents are not members of the State Retirement System coverage group and are therefore not covered under the State's § 218 agreement. Accordingly, for purposes of determining § 218 agreement coverage, it is irrelevant whether the medical residents were students within the meaning of § 210(a)(10) of the Act.

If the services of a state and local government employee, such as a medical resident, are not covered under the state's § 218 agreement, those services will be generally be covered under the FICA unless the employee is a member of a state retirement system.[4] Since the University medical residents are not members of the State Retirement System, a resident's services would generally be covered under the FICA unless the student FICA exception requirements are met.

The Employer Status and Student Status Requirements

Under § 3121(b)(10), the Student FICA exception is available only with respect to services performed in the employ of a S/C/U or a related § 509(a)(3) organization. Section 31.3121(b)(10)-2(d) of the regulations provides that the term "school, college, or university" for purposes of the student FICA exception is to be

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[3]Section 210(a)(10) of the Act is the parallel provision to § 3121(b)(10) of the Code.

[4]I.R.C. § 3121(b)(7)(F) (effective with respect to services performed after July 1, 1991).

construed in its “commonly or generally accepted sense.” A medical school will clearly qualify as a S/C/U. However, if the hospital where services are performed is the common law employer, the question arises whether the hospital qualifies as a S/C/U or a related § 509(a)(3) organization.

In addition to the employer status requirement, a resident with respect to whom the refund claim is filed must be a student who is enrolled and regularly attending classes at the S/C/U. Section 31.3121(b)(10)-2 of the regulations provides that whether an employee has the status of a student is determined on the basis of the employee's relationship with the S/C/U for which the services are being performed. An employee who performs services in the employ of a S/C/U as an incident to and for the purpose of pursuing a course of study at the S/C/U has the status of a student in the performance of those services. If an employee has the status of a student, then the amount of remuneration for services performed by the employee, the type of services performed by the employee, and the place where the services are performed are immaterial for purposes of the student FICA exception.

The National Office is developing further guidance on these issues.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

[redacted]

[redacted]

Please call if you have any further questions.

Jerry E. Holmes

CHIEF, BRANCH 2
(Employee Benefits and
Exempt Organizations)