



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

CHIEF COUNSEL

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[REDACTED]

Attention: [REDACTED]

Dear [REDACTED]:

I apologize for the delay in responding to your inquiry of November 24, 2003, on behalf of [REDACTED]. [REDACTED] wrote to you about the status of her refund claim for taxes she paid under the Federal Insurance Contributions Act (FICA) on remuneration for her services as a medical resident.

We received many refund claims as a result of the Eighth Circuit's decision in *State of Minnesota v. Apfel*, 151 F.3d 742 (8<sup>th</sup> Cir. 1998). In *State of Minnesota v. Apfel*, the Eighth Circuit held that medical residents the University of Minnesota employed in its residency programs were students within the meaning of the Social Security Act. Therefore, they did not need to pay FICA tax on their wages. Many institutions, and some individuals, have filed claims for refund because of this decision.

### **The Student FICA Exception**

The refund claims are based on section 3121(b)(10) of the Internal Revenue Code (Code) that says services students perform are excepted from FICA taxes. The Code defines a student as an individual employed by a school, college, or university at which he or she is enrolled and regularly attends classes. The student FICA exception applies only to services performed in the employ of an organization that has the status of a school, college, or university (SCU); and only if the student who performs the services is enrolled and regularly attends classes at that school, college or university.

Organizations like hospitals typically conduct noneducational and educational activities. The IRS has maintained administratively that the primary purpose of the organization determines whether it is a SCU for purposes of the student FICA exception. However,

the court rejected this argument in *United States v. Mayo Foundation*, 282 F. Supp. 2d 997 (D. Minn. 2003).

Before taking action on the refund claims, we studied whether the performance of certain services that are typically on-the-job training, like the services performed by medical residents, are excepted from employment under the student FICA exception; and whether organizations that conduct noneducational and educational activities, like hospitals, are SCUs within the meaning of section 3121(b)(10) of the Code. Accordingly, we suspended the refund claims while we considered a sample of the claims involving medical and dental residents and interns. Our goal was to apply our conclusions from the sample cases to refund claims involving similar residency programs to ensure we consistently applied the law and minimized taxpayer burden that would result if we examined each claim.

### **The Proposed Regulations**

After we carefully considered the refund claims and litigation of the student FICA exception, we determined that additional guidance is needed to provide greater clarity for the future. Accordingly, on February 24, 2004, the IRS proposed amendments to the Employment Tax Regulations interpreting section 3121(b)(10) of the Code. [see proposed regulations section 31.3121(b)(10)-2(c), (d), and (e) published in the Federal Register on February 25, 2004 (69 Fed. Reg. 8604)]. The regulation provides more detailed standards for determining what is a SCU and who is a student within the meaning of section 3121(b)(10) of the Code. The regulations, as proposed, apply to services performed on or after February 25, 2004. As soon as the regulations were issued, we turned our attention to resolving the large inventory of pending refund claims.

### **The Resolution of Existing Claims**

We are aware that many hospitals and individuals have filed claims for refund pertaining to services performed before February 25, 2004. The IRS is currently evaluating a resolution approach that could enable taxpayers to resolve past tax periods without further delay or burden. Clearly, such a program needs to be appropriately crafted and equitable amongst similarly situated taxpayers. We expect further information will be available in May; in the interim, we appreciate the patience of your constituent.

We will make this letter available for public inspection after we delete names, addresses, and other identifying information, as appropriate, under the Freedom of Information Act.

I hope this information is helpful. If you have any additional questions or we may assist you further, please contact me or [REDACTED] (ID# [REDACTED]) at [REDACTED].

Sincerely,

Sarah Hall Ingram  
Division Counsel/ Associate Chief Counsel  
Tax Exempt and Government Entities