

IRS TO HONOR MEDICAL RESIDENT FICA REFUND CLAIMS

Young physicians who paid Federal Insurance Contributions Act (FICA) taxes as medical residents in recent years may see their refund claims honored by the IRS. For more than a decade, most teaching hospitals in the United States and some individual taxpayers (including medical residents) have had refund claims pending with the Internal Revenue Service (IRS) for FICA taxes paid as a result of a “student exception” under Internal Revenue Code 3121 (b)(10).

FICA is a United States payroll tax, imposed by the federal government, on both employees and employers to fund Social Security and Medicare and are withheld from and employee’s pay at a rate of 7.65% on gross earnings (6.2% for Social Security and 1.45% for Medicare). The employer is also liable for the same, making the total Social Security tax 12.4% and the total Medicare tax 2.9% of wages.

As a result, on a \$50,000 annual stipend, \$3,825 in FICA tax would have been paid by both the medical resident and their teaching hospital, for a total of \$7,650. Therefore, if we assume a four year dermatology residency, with no increase in stipend, the potential refund would amount to a total of \$30,600 (\$15,300 for the medical resident and \$15,300 for the teaching hospital).

Often schools, colleges and universities employ students on a part-time or intermittent basis. Many of these students qualify for a statutory exception to FICA taxes, and those work periods are not credited to the earning of Social Security and related benefits.

The IRS has consistently urged that the “student exemption” from FICA be narrowly construed. In two cases decided in the mid 1990s where two institutions

had sued to recover a refund of FICA taxes paid, the question arose whether employees performing services in the nature of on-the-job training are students and thus exempt from FICA.

The University of Minnesota claimed that residents working in a hospital setting can qualify for the student exemption, and won both in the federal district court and the Eighth Circuit Court of Appeals. The second institution, Mayo Clinic, won a similar refund claim in the same Minnesota federal district court.

In response, the IRS further tightened regulations in late 2004 to restrict the use of the “student exemption.” On April 1, 2005, new regulations regarding the student FICA exception became effective. One part of these regulations states that an employee who works 40 hours or more (full-time employee) for a school, college or university is not eligible for the student exception. This part of the regulations excludes medical residents from the student exception.

On March 2, the IRS announced that it has made an administrative determination to accept the position that medical residents are exempted from FICA taxes based on the student exception for tax periods ending before April 1, 2005, when new IRS regulations went into effect.

Since the statute of limitations for filing a claim for tax periods prior to April 1, 2005

has expired, it is too late to file a claim for periods before April 1, 2005.

However, if you are or were a medical resident and you did not file an individual FICA refund claim, you may be covered by a FICA refund claim filed by your employer for the period during which you were a medical resident. You would need to contact your employer (or former employer) to see if they filed a FICA refund claim on your behalf.

For more information, call (800) 919-1703 or visit www.irs.gov/charities and click on Medical Resident FICA Refund Claims.

Taxpayers with currently pending suits should contact the Department of Justice attorney assigned to the case.

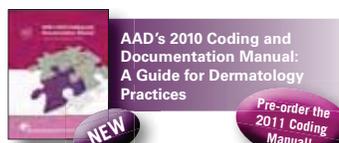
The IRS has indicated that within 90 days it will begin contacting hospitals, universities and medical residents who filed FICA refund claims for these periods with more information and procedures. Thus, employers and individuals with pending claims do not need to take any action at this time.

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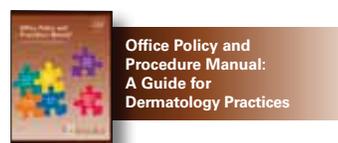
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