

Supreme Court Upholds IRS, Strikes Blow for Medical Residents

By Brian Mahany

On January 11th, the U.S. Supreme Court dealt a major victory to the IRS. The court unanimously ruled that medical residents are full time employees and not subject to special exemptions reserved for students.

Since 1951, the Treasury Department has construed the student exemption to exempt from taxation students who work for their schools "as an incident to and for the purpose of pursuing a course of study." In 2004, the IRS changed the rule that said medical residents were entitled to the student exemption. The Service ruled that doctors in training must pay social security and Medicare FICA taxes.

The 2004 rule change generated the case that ultimately made it to the Supreme Court. Unfortunately for doctors, the court ruled in favor of the IRS. The rule change is expected to generate an estimated \$700 million in new annual revenues.

The IRS rule now says that students are no longer exempt if they work full time as part of their study program. Medical residents typically work 50 to 80 hours per week.

Even though medical residency is mandatory for physicians and involves intense training, the IRS ruled that the residents were not students for tax law purposes. The residency program for newly graduated doctors is where most learn their specialty. For example, to become a neurologist, a person must first get their medical degree and then attend a residency program in a hospital neurology program.

The IRS has elected to apply the new rule effective April 1st, 2005. Physicians who haven't paid in hopes of a court victory should expect large assessments for back taxes, interests and penalties.

The case is Mayo Foundation for Medical Education and Research v. United States.

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Brian Mahany is a lawyer and partner at Mahany & Ertl, LLC in Milwaukee, Wisconsin. He concentrates in tax litigation, criminal tax defense and audit defense. Brian can be reached at (414) 704-6731 (direct) or through his website, <http://www.mahanyertl.com>