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Supreme Court Medical Resident Stipend Ruling Highlights Advisability of Health Care, Other Employer Review of Worker Classification, Payroll Practices

Stipends paid to medical residents to provide on patient care and other medical services for 40 or more hours per week as part of an accredited graduate medical education program are wages paid to employees for Federal Insurance Contributions Act (FICA) payroll taxes purposes and do not qualify as exempt from FICA tax or withholding as student stipends according to January 11, 201 U.S. Supreme Court ruling in **Mayo Foundation v. U.S.** The decision is the latest reminder to health care providers and others of the need to critically review and update as necessary their organizations existing worker and wage characterization in light of evolving interpretations and the growing success of regulators and private plaintiffs in challenging these classifications.

Mayo Foundation Decision

The FICA rules set forth in Internal Revenue Code (Code) §§3101(a) and 3111(a) require that employees and employers pay FICA taxes on all "wages" employees receive not otherwise exempted. In *Mayo Foundation*, Mayo Foundation For Medical Education And Research (Mayo) challenged a 2004 Internal Revenue Service (IRS) Regulation challenged a 2004 IRS regulation that ruled that medical students or others providing full-time services as part of their course of instruction do not qualify as "students" for purposes of the "student" exemption of Code § 3121(b)(10).

Code Section 3121(b)(1) excludes from FICA wages of amounts paid "service performed in the employ of . . . a school, college, or university . . . if such service is performed by a student who is enrolled and regularly attending classes at [the school]." Mayo Foundation filed suit after the IRS changed its historical interpretation of Code § 3121(b)(10). Prior to 2004, the applicability of the Code § 3121(b)(10) exclusion was determined subjectively using a facts and circumstances analysis.

In December, 2004, however, the IRS amended its regulations to provide that an employee's service is "incident" to his studies only when "[t]he educational aspect of the relationship between the employer and the employee, as compared to the service aspect of the relationship, [is] predominant." See Treas. Reg. §31.3121(b)(10)–2(d)(3)(i). The Regulation, which remains in effect today, also contains a "Full-Time Employee Rule": that categorically provides that"[t]he services of a full-time employee "are not incident to and for the purpose of pursuing a course of study regardless of the fact that "the services performed . . . may have an educational, instructional, or training aspect." See Treas. Reg.§31.3121(b)(10)–2(d)(3)(iii). The Full-Time Employee Rule specifies that which workers qualify as full-time generally is as defined by the employer's policies, but in any event includes any employee normally scheduled to work 40 hours or more per week. In the case of "Employee E," who is employed by "University V" as a medical resident, Example 4 of the Full-Time Employee Rule states that Employee E is not an exempt student under Code § 3121(b)(10) because his "normal work schedule calls for [him] to perform services 40 or more hours per week."

The Supreme Court rejected Mayo Foundation's arguments. It ruled that IRS' interpretation of Code § 3121(b)(1) as inapplicable to medical students or other workers providing full-time services as part of a residency or other educational program should stand because Congress has not directly spoken to foreclose that interpretation and because the Treasury Department's rule is a reasonable construction of what Congress has said.

Worker Classification Growing Risk For Health Care & Other Industries

Beyond its specific holding, the *Mayo Foundation* decision also serves as another reminder that health industry and other employers should not take the defensibility of their worker classification and associated income and payroll tax, employee benefit, employment and other practices for granted. Recent developments send a clear message that

health industry and other employers must remain constantly diligent about confirming and documenting the defensibility of their worker classifications and other associated practices in light of evolving rules and standards, enforcement, the growing frequency and success of regulators and private plaintiff challenges, and changing workforce practices. See e.g. **Review of Worker Classification Needed As Classification Scrutiny Rises**;**Minimum Wage, Overtime Risks Highlighted By Labor Department Strike Force Targeting Residential Care & Group Homes**; **Review & Strengthen Defensibility of Existing Worker Classification Practices In Light of Rising Congressional & Regulatory Scrutiny**; **250 New Investigators, Renewed DOL Enforcement Emphasis Signal Rising Wage & Hour Risks For Employers**; **Quest Diagnostics, Inc. To Pay $688,000 In Overtime Backpay**.

Tax, labor and other federal and state regulators are stepping up their scrutiny of health industry and other employer practices for classifying workers under existing laws. Under an ongoing National Research Program, for instance, the Internal Revenue Service has begun conducting the first of approximately 6,000 payroll tax audits that it plans to complete over a three-year period focusing on the appropriateness of employer worker classification and other payroll tax practices. Department of Labor officials also have stepped up scrutiny of and challenges to employer characterizations of workers as contractors, exempt, or otherwise not covered by wage and hour, discrimination, and other employment and employee benefit laws and have announced plans to further tighten existing rules. For instance, the Labor Department Wage & Hour Division has announced plans to tighten Fair Labor Standards Act (FSLA) recordkeeping and reporting requirements to require, among other things that employers who wish to classify any employee as "exempt" from the overtime provisions of the FLSA or who wish to set up a relationship with a worker as an "independent contractor" engage in significant analysis and be able to provide proof that they have classified those relationships accurately. As other agencies and private plaintiff's follow suit, legislation that would further tighten worker classification rules continues to enjoy broad support among many members of Congress.

In light of these and other developments, health industry and other employers should take reasonable steps to guard against these and other growing risks of worker misclassification and associated non-compliance. To minimize their potential exposure, health industry and other employers should consult with qualified legal counsel for advice within the scope of attorney-client privilege concerning the need to audit or otherwise act to strengthen the defensibility of their existing worker classification, employee benefit, fringe benefit, employment, wage and hour, and other workforce policies to mitigate exposures to potential IRS, Labor Department or other risks of worker misclassification or the handling of associated payroll, employment or other responsibilities.

For Help With Investigations, Policy Updates Or Other Needs

If you need assistance in conducting a risk assessment of or responding to an IRS, Labor Department or other legal challenges to your organization's existing workforce classification or other labor and employment, employee benefit or compensation practices, please contact the author of this update, attorney Cynthia Marcotte Stamer **here** or at (469)767-8872 .

Board Certified in Labor & Employment Law by the Texas Board of Legal Specialization, management attorney and consultant Ms. Stamer is nationally and internationally recognized for more than 23 years of work helping employers; employee benefit plans and their sponsors, administrators, fiduciaries; employee leasing, recruiting, staffing and other professional employment organizations; and others design, administer and defend innovative workforce, compensation, employee benefit and management policies and practices. The Chair of the American Bar Association (ABA) RPTE Employee Benefits & Other Compensation Committee, a Council Representative on the ABA Joint Committee on Employee Benefits, Government Affairs Committee Legislative Chair for the Dallas Human Resources Management Association, past Chair of the ABA Health Law Section Managed Care & Insurance Interest Group, and the Managing Editor of **Solutions Law Press HR & Benefits Update** and other Solutions Law Press Publications, Ms. Stamer recently was a featured panelist on the ABA Joint Committee on Employee Benefits Teleconference on "Worker Classification & Alternative Workforce: Employee Plans & Employment Tax Challenges" and has worked, published and spoken extensively on worker classification and other related matters. She also is recognized for her publications, industry leadership, workshops and presentations on these and other human resources concerns and regularly speaks and conducts training on these matters. Her insights on these and other matters appear in the Bureau of National Affairs, Spencer Publications, the Wall Street Journal, the Dallas Business Journal, the Houston Business Journal, and many other national and local publications. For additional information about Ms. Stamer and her experience or to access other publications by Ms. Stamer see **here** or contact Ms. Stamer directly.

Other Helpful Resources & Information

If you found this article of interest, you also may be interested in reviewing other Breaking News, articles and other resources available **here** including:

- **Minimum Wage, Overtime Risks Highlighted By Labor Department Strike Force Targeting Residential Care & Group Homes**
- **Health Care Fraud Enforcement Packs New Heat**
- **President Signs Long-Sought Red Flag Rule Exemption Into Law**
- **Quality, Recordkeeping & Unprofessional Conduct Lead Reasons For Medical Board Discipline of Physicians**
- **CMS Finalizes Calendar Year 2011 Physician Fee Schedule & Other Medicare Part B Payment Policies**
- **DEA Cautions Practitioners Must Restrict Delegation of Controlled Substance Prescribing Functions, Urges Adoption of Written Policies & Agreements**
- **Avoiding Post-Holiday Celebration Sexual Harassment & Discrimination Liability**
- **Small Employers Should Weigh If Health Premium Tax Credit Justifies Changing Employee Leasing Arrangements**
- **2011 Standard Mileage Rates Announced**
- **Update Employment Practices To Manage Genetic Info Discrimination Risks Under New EEOC Final GINA Regulations**
- **EEOC Attacks Medical Leave Denials As Prohibited Disability Discrimination**
- **New Insured Group Health Plan Non-Discrimination Rules Create Significant Liability For Employers & Insurers; Prompt IRS Also To Review Self-Insured Group Health Plan Rules**
- **Affordable Care Act's Health Plan External & Internal Review Safe Harbor & Other Regulations Require Health Plan Updates**
- **New Rule Requires Federal Government Contractors To Post New "Employee Rights Under The National Labor" Poster**
- **Employers Concerned About New Union Powers As NLRB Orders Union Elections In 31 California Health Care Facilities To Proceed**

If you or someone else you know would like to receive future updates about developments on these and other concerns, please be sure that we have your current contact information – including your preferred e-mail – by creating or updating your profile **here**. For important information concerning this communication click **here.** If you do not wish to receive these updates in the future, unsubscribe by updating your profile **here.**