IRS Student FICA Guidelines

Overview

The Internal Revenue Service (IRS) issued new guidelines setting forth the standards to use to determine whether student employees are eligible for the "safe harbor" student FICA Exemption, on December 21, 2004. These standards apply to institutions of higher education meeting the necessary requirements. Guidelines were issued in Revenue Procedure 2005-11 (Rev. Proc. 2005-11) for services performed on or after April 1, 2005. This revenue procedure modifies the "safe harbor" FICA exemption standards provided in Rev. Proc. 98-16. Midwestern State University follows the IRS rules in determining a student's exemption from FICA withholding. Following are the highlights of the IRS revenue ruling and Midwestern State University procedures.

Note: For discussion purposes, the term FICA (Federal Insurance Contributions Act) will be used to identify both portions of the tax, social security (OASDI) and Medicare. When eligible, OASDI is withheld at a rate of 6.2% and Medicare at 1.45% for a total of 7.65% withholding rate.

Student Status - General Rule

In order to have the status of a student, the employee must be enrolled and regularly attending classes in pursuit of a course of study. In addition, the employee's services must be incident to and for the purpose of pursuing a course of study. The educational aspect of the relationship between the employer and the employee must be predominant in order for the employee's services to be incident to and for the purpose of pursuing a course of study.

Applicable Credit Hour Standards for Undergraduate and Graduate Students

An individual who is a half-time undergraduate student or a half-time graduate student will qualify for the Student FICA exception under this revenue procedure with respect to services performed at or for institutions of higher education in which they are enrolled.

At Midwestern State University the half-time student qualifications are:

- Undergraduate Student – 6 credit hours (3 credit hours per term during summer)
- Graduate student - 3 credit hours

Full-time Employee Not Eligible for Exemption

Services provided by a full-time employee are ineligible for the student FICA exception. The final regulations provide that full-time services are not incident to and for the purpose of pursuing a course of study. However, whether an employee is full-time is based on the employer's standards and practices. Except that employees whose normal work schedule is 40 hours or more a week are considered full-time employees. But, the final regulations provide that an employee's work schedule on an occasional basis or during an academic break are not considered in determining whether the employee's normal work schedule is 40 hours or more per week.

Professional Employees

The safe harbor FICA exemption is normally disallowed with respect to professional employees whose work requires knowledge of an advance type in a field of science or learning, requires the consistent exercise of discretion and judgment, and is predominantly intellectual and varied in character. However, some professional employees may qualify for the student FICA exception based on consideration of all the facts and circumstances.

Career Employees Not Eligible for Exemption

According to the IRS revenue procedure, career employees are not eligible for the student FICA exemption because their employment cannot be considered to be incident to and for the purpose of pursuing a course of study. The guidelines define career employees as those who meet the following tests:

- Eligible to participate in a retirement plan (i.e. MSRS, Faculty Retirement Plan, 403(b) optional retirement plan, 457 deferred compensation plan),
- Eligible for vacation, sick leave, or paid holiday benefits,
- Eligible to receive tuition waiver benefits (other than the qualified tuition reduction under section 117(d)(5) of the Code provided to teaching or research assistants) or,
- Eligible to receive benefits under sections 79 (life insurance), 127 (educational assistance), 129 (dependent care),
- Classified as a career employee by the institution.
• If the employee performs services in multiple jobs, the employee will be considered a career employee if any one of the jobs is deemed that of a career employee.

### Students Working at the Beginning or End of an Academic Term

The IRS states in the revenue procedure that a pay period that falls fully or partially within an academic term will be eligible for the FICA exemption. At Midwestern State University, if the academic term begins at any point within a pay period, the entire period is considered for the exemption, not just the days actually within the term.

For example: Pay period begins on August 11th and ends on September 10th and the term begins on September 4th, the entire pay period from the 11th through the 10th would be exempt from FICA if the student otherwise qualified for the exemption.

### Breaks of Under or Over Five Weeks

The student FICA exemption does not apply to services performed by a student who is not enrolled in classes during school breaks of more than five weeks (including summer breaks of more than five weeks). However, if the school break is less than five weeks in duration, the student may still be eligible for the exemption if enrolled in classes just prior to the break, and eligible to be enrolled in classes following the break. The new guidelines in Rev. Proc. 2005-11 reaffirm the IRS position on FICA eligibility during breaks between semesters.

**Example - break less than 5 weeks in duration**

A student is registered for Fall semester (classes beginning August 25th and ending December 14th), and is eligible to register for Spring semester (classes beginning January 13th). Since the break between Fall and Spring semester is less than 5 weeks (December 15th and through January 13th), the student is eligible for the Student FICA exemption.

**Example - break of more than 5 weeks**

A student is registered for Spring semester (beginning January 13th and ending May 11th), and is eligible to register to Fall semester (beginning August 25th). However, the student is not registered for summer session, but continues to work through the summer in a student position. The student is subject to FICA withholding during the summer since the break between Spring semester and Fall semester is more than 5 weeks in duration.

### Anti-Abuse Rule

The standards in this revenue procedure must be applied in a reasonable manner, consistent with the purpose of excluding from employment only services that are performed as an incident to and for the purpose of pursuing a course of study at an institution of higher education. Section 9 of the IRS guidelines in Rev. Proc. 2005-11 gives the IRS the authority to ignore the FICA exemption in this revenue procedure under certain circumstances. The anti-abuse rule would apply if the institution "inappropriately" applied the guidelines so as to manipulate or mischaracterize the nature of the relationship between an employee and institution so as to avoid the payment of FICA taxes.

Following are two examples given in the revenue procedure where the anti-abuse rule applies:

• The standards would be inappropriately applied through the manipulation of the relationship between employees and the institution if a university claimed that the Student FICA exemption applied to research laboratory workers, who had been career employees, but were converted to non-career status and required to enroll in a certificate program granting six credit hours per semester for work experience in the laboratory.

• As another example, if an individual who was not a student worked for a university on a full-time basis for many years, in a job generally performed by non-students, and then enrolled at the university for six credit hours of course work per semester while continuing the full-time work in the same job, it is not appropriate to apply the standards of Rev. Proc. 2005-11 to conclude that the employee's work has suddenly "become incident to and for the purpose of pursuing a course of study" solely because the employee enrolled in coursework.