

# SUPERCEDED BY HR 2005-28

THE CALIFORNIA STATE UNIVERSITY  
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**Date:** March 25, 2005

**Code:** HR 2005-14

**To:** CSU Presidents

Supersedes: HR 1996-08  
HR/PCOS 1996-01  
HR/Benefits 1998-05  
HR/Benefits 1996-07  
HR/Benefits 1992-20

**From:** Jackie R. McClain  
Vice Chancellor  
Human Resources



**Subject:** Student Employment and the Student FICA Exemption

Internal Revenue Service (IRS) Code Section 3121(b)(10) excludes services performed by students employed by a school, college or university from Social Security and Medicare (FICA) coverage. On December 21, 2004, the IRS issued final regulations amending §3121(b)(10) and **these regulations are applicable for services performed on or after April 1, 2005**. These new regulations plus Revenue Procedure 2005-11, which provides safe harbor standards used in determining if employees are eligible for the student FICA exemption, and a supplemental information document, are available at: <http://www.irs.gov>. Revenue Procedure 2005-11 modifies the safe harbor standards of Revenue Procedure 98-16, which your campus has been relying on to determine student employment FICA decisions. The IRS has advised that the campus may rely on Revenue Procedure 98-16 with respect to services performed prior to April 1, 2005.

The following current and consolidated student employment and FICA exemption information is provided for reference:

Attachment A: General Guidance: Student Employment and the Student FICA Exemption

Attachment B: - Processing Information for Non-Represented Excluded (E99) Student Assistants, including "Bridge" Students, Resident Assistants, and students in a non-resident alien status  
- Processing Information for represented Instructional Student Assistants, Graduate Assistants and Teaching Associates in Unit 11 (UAW)

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**Distribution:**

CSU Presidents  
Vice Presidents, Academic Affairs  
Vice Presidents, Administration  
Vice Presidents/Deans of Students

Budget Managers  
Benefits Officers  
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Director, SOSS

Attachment C: IRS Code Section 3121(b)(10) and Revenue Procedure 2005-11

Attachment D: Code of Federal Regulations section 674.2

Attachment E: FICA Coverage Decision Chart

Attachment F: Teaching Associate Facts and Circumstances Test Examples

Questions regarding this document may be directed to Human Resources Administration at (562) 951-4411. This document is available on the Human Resources Web site at: <http://www.calstate.edu/HRAdm/memos.shtml>.

JRMcC/cr

Attachments

## **GENERAL GUIDANCE: STUDENT EMPLOYMENT AND THE STUDENT FICA EXEMPTION**

**NOTE:** CSU's current policy regarding Use of Student Assistant Classifications (FSA 81-13, Supplement No. 1) notes that with the exception of student appointments to Work-Study classifications, when school is in session, Student Assistants may work up to 20 hours per week, but normally would not work in excess of 20 hours per week, except under emergency or other unusual situations. In the following guidance on the student FICA exemption, you will note the Internal Revenue Service (IRS) states that student employees may work up to 40 hours per week and if certain facts and circumstances are met they could qualify for the student FICA exemption. That IRS work schedule guideline does not override CSU's employment policy for student employees as noted above. CSU's 20-hour guideline is specific to CSU policy, not tied to IRS regulations.

- FICA refers to both Social Security and Medicare. IRS Code Section 3121(b)(10) excludes services performed by students employed by a school, college or university from FICA coverage. This exclusion is referred to as the "student FICA exemption."
- Teaching Associates (TAs) who are eligible to participate in CalPERS retirement also correspondingly participate in Social Security. These TAs do not qualify for the student FICA exemption.
- The IRS looks to key criteria summarized below to determine if a student qualifies for the student FICA exemption (refer to 3121(b)(10) regulations and Revenue Procedure 2005-11 for specifics and the IRS supplementary information):
  - ✓ The IRS looks at the relationship of the employee to the university. To have student status, the employee must perform services in the employ of the university at which the employee is enrolled and regularly attending classes in pursuit of a course of study. A class is an instructional activity led by a faculty member or other qualified individual following an established curriculum.
  - ✓ The employee's services must be incident to and for the purpose of pursuing a course of study in order for the employee to have the status of student.
  - ✓ The educational aspect of the relationship between the employer and the employee, as compared to the service aspect of the relationship, must be predominant for the employee's services to be incident to and for the purpose of pursuing a course of study. The educational aspect is evaluated based on all relevant facts and circumstances related to the educational aspect of the relationship and the service aspect is evaluated based on relevant facts and circumstances related to the employee's employment.
  - ✓ Student status is determined with respect to each academic term.
  - ✓ Full-time employees are not eligible for the student FICA exemption regardless of whether they are full-time or half-time students because by definition, the employee's services are not incident to and for the purpose of pursuing a course of study. A full-time employee is an employee whose normal work schedule is 40 or more hours per week. Work schedule is determined at the start of an academic term. A person's work schedule during an academic break is not considered in determining whether the person's normal work schedule is 40 or more hours per week.

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- ✓ **For full-time students**, who are not full-time employees, a facts and circumstances test determines whether or not the employee is eligible for the student FICA exemption. If the educational relationship between the employee and the university is predominant as opposed to the service relationship, the student FICA exemption will apply. A fact and/or circumstance may be a relevant factor, but may not be a dispositive criterion in determining whether or not the employee qualifies for the student FICA exemption. The facts and circumstances that need to be considered are:
  - Course workload relative to a full-time course workload at the campus.
  - Normal work schedule and hours actually worked.
  - Whether the employee has the status of a professional employee, as that suggests that the service aspect of the employee's relationship with the employer is predominant.
  - Whether the employee is required to be licensed to work in a field in which the person performs services. If an employee is licensed, that suggests that the service aspect of the employee's relationship with the employer is predominant.
  - Whether the employee is eligible to receive certain benefits, including vacation, paid sick leave, paid holidays, life insurance, qualified educational assistance, dependent care assistance, adoption assistance or whether the employee is eligible to participate in any 401(a), 403(b) or 457 retirement plans. Eligibility for benefits mandated by law is given a lesser amount of weight in evaluating the relationship. Health benefits are not considered. Eligibility to participate in a retirement plan is generally more significant than eligibility to receive a dependent care employment benefit. Additional weight is given to the fact that an employee is eligible to receive an employment benefit if the benefit is generally provided to persons in positions generally held by non-students.
  - Whether the employee is eligible for reduced tuition (other than qualified tuition reduction under IRC 117(d)(5) provided to a teaching or research assistant who is a graduate assistant) because of the employee's relationship with the institution.
- ✓ **For half-time undergraduate or half-time graduate or professional students**, who are not full-time employees, a "safe harbor" test determines whether or not the employee is eligible for the student FICA exemption. If an employee does not meet the "safe harbor" test, the employer next shall use the facts and circumstances test described above for full-time students to determine FICA eligibility. Half-time students are eligible for the "safe harbor" FICA exemption, provided:
  - They are not full-time employees.
  - They are not professional employees.
  - They do not receive any of the benefits described above (eligibility for health benefits or benefits mandated by law will not disqualify a half-time student from the safe harbor).
  - They are not otherwise considered a career employee by the university.

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- Full-time undergraduate and half-time undergraduates are defined by the Department of Education regulations at 34 C.F.R. § 674.2. (See Attachment D.) Graduate and professional students and half-time graduate and professional students are defined in Section 8.03 and 8.04 of Rev. Proc. 2005-11. Additionally, an individual is considered to be a half-time undergraduate and half-time graduate and professional student if he/she is not a career employee and carries less than a half-time academic workload as determined by the campus standards and practices in his/her last semester, trimester or quarter of a course of study requiring at least 2 semesters, trimesters, or quarters to complete and is enrolled in the number of hours needed to complete the requirements for obtaining a degree.
- The student FICA exemption does not apply to less than half-time undergraduates and less than half-time graduate and professional students, except as noted in the bullet above.
- According to the IRS, services performed by the student employee are eligible for the student FICA exemption with respect to all services performed during all pay periods of a month or less that fall wholly or partially within the academic term.
- The determination of student status should be made at the end of the drop-add period and may be adjusted thereafter at the campus option. The determination of student status for payroll periods ending before the end of the drop-add period may be based on the number of semester, trimester or quarter hours being taken at the end of the registration period for that semester, trimester or quarter.
- The student FICA exemption applies to student employment, which continues during normal school breaks of five weeks or less, provided the individual was eligible for the student FICA exemption on the last day of classes or examinations preceding the break and is eligible to enroll in classes for the first academic period following the break.
- The student FICA exemption does not apply to services performed by an individual who is not enrolled in classes during breaks of more than five weeks, including summer breaks of more than five weeks or during a single quarter break on a quarter year-around campus.
- Student employment that does not qualify for the student FICA exemption requires Social Security and Medicare participation, but the Omnibus Budget and Reconciliation Act (OBRA) permits the employer to provide an alternate mandatory retirement plan in lieu of Social Security. The CSU uses the Department of Personnel Administration's Part-time, Seasonal and Temporary (DPA PST) Plan for student employees who do not qualify for the student FICA exemption. The CSU alternative OBRA plan requires the student employee to pay 7.5% of all earnings to the retirement plan. Additionally, student earnings are subject to Medicare taxes, currently 1.45% of all earnings, paid by both the student and the employer.
- If a student qualifies for the student FICA exemption during the academic year, but not during the academic break, the mandatory retirement plan participation dates are determined by the respective campus' academic calendar.

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- Employment appointments during “break” periods that do not qualify for the student FICA exemption or employment appointments for less than half-time students will be to the non-represented “bridge” classification or the represented Instructional Student Assistant, Graduate Assistant or Teaching Associate classifications, as appropriate, with the correct Retirement Account Code (PIMS Item 505) to denote mandatory retirement plan participation (in lieu of Social Security) plus Medicare. Refer to the processing instructions in Attachment C for more information.
- Employment that qualifies for the student FICA exemption generally also meets the Unemployment Code Section 642 exclusion from unemployment insurance coverage. Employment that is not excluded from FICA coverage will generally be covered by unemployment insurance.

## PROCESSING INFORMATION FOR EXCLUDED (E99) STUDENT CLASSIFICATIONS:

- **Student Employment Classifications – FICA/OBRA Excluded**

1870: Student Assistant  
1871: Student Trainee, On-Campus Work Study  
1872: Student Trainee, Off-Campus Work Study  
1869: Resident Assistant

FICA Exclusion: Appointments to the classifications noted above qualify for the student FICA exemption pursuant to IRS Code Section 3121(b)(10). Students in these classifications do not pay Social Security or Medicare, nor are they enrolled in the DPA PST plan in lieu of Social Security.

Appointment Information: Student appointments in classifications 1870, 1871, and 1872 are placed on the PIMS employment history database via a “shell” A98 transaction. This appointment structure does not allow for the withholding of retirement plan participation, including FICA. Resident Assistants are appointed on the PIMS employment history database via an A52 transaction with the Retirement Account Code (PIMS Item 505) set at “N.”

- **Other Student Employment Classifications – FICA/OBRA Covered**

1874: “Bridge” Student Assistant  
1875: “Bridge” Student Trainee, On-Campus Work-Study  
1876: “Bridge” Student Trainee, Off-Campus Work-Study  
0100: Youth Summer Aid<sup>1</sup>

FICA Covered (Student is enrolled in DPA PST in lieu of Social Security plus Medicare): “Bridge” classifications are available to accommodate CSU student employment that does not qualify for exclusion from Social Security/Medicare. The “bridge” classification is available for student employment during academic breaks and/or student employment during academic terms when the student is less than a half-time student. For student “bridge” and Youth Summer Aid appointments, student employees are required to participate in Medicare and a mandatory retirement plan in lieu of Social Security.

Appointment Information:

Appointments to “bridge” and the Youth Summer Aid classifications are processed as temporary hourly intermittent appointments via an A52 transaction.<sup>1</sup>

Appointments must indicate a Retirement Account Code (PIMS Item 505) reflecting the DPA PST (in lieu of Social Security) and Medicare participation. The correct code will generally be “TM” which indicates the student is covered by Medicare. (Note: code “TD” would be used if the student is NOT covered by Medicare because s/he has been continuously employed with the CSU since prior to April 1, 1986.)

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<sup>1</sup> Previously, the Youth Summer Aid classification (0100) was appointed via an A98 transaction and FICA was not withheld. Campuses should now use the A52 transaction and Retirement Account Code, as indicated above.

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Unlike appointments processed on “shell” A98 transactions (for codes 1870, 1871 and 1872), the “bridge” and Youth Summer Aid appointments require the campus to process a separation transaction (S31) when the student leaves employment or switches to other CSU employment status.

A student in the “bridge” classification code can have multiple appointments at different rates of pay. In instances where the position number stays the same, campuses may request pay at different rates via PIP. In instances where the campus wants different rates issued from different position numbers, separate rosters must be established.

When the student changes from the “bridge” or Youth Summer Aid classification code to any other classification code, he/she is not eligible to withdraw his/her DPA PST funds until he/she separates from all CSU employment.

- **Student, Nonresident Alien Tax Status Classification**

1868: Student Nonresident Alien Tax Status

Appointments to the Student, Nonresident Alien Tax Status classification are exempted from FICA pursuant to IRS Code Section 3121(b)(19). Refer to Technical Letter HR/Salary 2004-02 for additional information (<http://www.calstate.edu/HRAadm/pdf2004/TL-SA2004-02.pdf>).



## PROCESSING INFORMATION FOR REPRESENTED STUDENT CLASSIFICATIONS:

- **UAW Student Appointments – (Unit 11)**

1150: Instructional Student Assistant

1151: Instructional Student Assistant, On-Campus Work-Study

2355: Graduate Assistant – Academic Year

2325: Graduate Assistant – Monthly

2326: Graduate Assistant – On-Campus Work-Study

2354: Teaching Associate – Academic Year

2353: Teaching Associate – 12 Month

FICA Exclusion: Instructional Student Assistants (ISAs), Graduate Assistants (GAs) and Teaching Associates (TAs) are exempt from FICA, provided the student meets the student FICA exemption addressed in Internal Revenue Code 3121(b)(10) during the academic term. (Please note that TAs who participate in CalPERS also participate in Social Security plus Medicare.)

FICA Covered (Student is enrolled in DPA PST in lieu of Social Security plus Medicare): Continuing ISAs, GAs and TAs who still qualify for an ISA or GA or TA appointment during breaks/summer term, but who no longer qualify for the student FICA exemption, must be placed in mandatory retirement plan participation (in lieu of Social Security) which, in this instance, is the DPA PST plan. Medicare withholding also is required. Additionally, ISAs, GAs and TAs who do not qualify for the student FICA exemption because they are less than half-time students during an academic term also must participate in the DPA PST Plan, plus Medicare. (Again, please note that TAs who participate in CalPERS also participate in Social Security plus Medicare.)

Appointment Information: ISAs are appointed in temporary hourly/intermittent appointments via an A52 transaction. Unlike non-represented Student Assistants (e.g., class code 1870) who are appointed on an A98 “shell” appointment, a separation (S31) transaction must be generated when the ISA terminates employment or changes to other CSU employment status.

GAs are appointed in temporary appointments via an A52 transaction. Timebase (PIMS Item 405) for a 20-hour per week appointment is set at full-time (FT).

TAs are appointed in temporary appointments via an A52 transaction. Timebase (Item 405) is set to any fraction less than full-time (HR 2002-06).

When the GA or ISA qualifies for the student FICA exemption, Retirement Account Code (PIMS Item 505) should be set at “N.”

When the TA qualifies for CalPERS retirement, Retirement Account Code (Item 505) should be set to “08.” Otherwise, if the TA qualifies for the student FICA exemption, Retirement Account Code should be set at “N.”

When the GA, TA or ISA no longer qualifies for the student FICA exemption, as outlined above under the FICA Covered section, the following appointment procedures are provided:

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- ISAs remain in the ISA classification. However, campuses must change Retirement Account Code (PIMS Item 505) from “N” to “TM” to trigger DPA PST (in lieu of Social Security) and Medicare withholding.
- GAs and TAs in the Monthly classifications (code 2325 and 2353) remain in the Monthly classification. Like ISAs, campuses must change Retirement Account Code (PIMS Item 505) from “N” to “TM” to trigger DPA PST (in lieu of Social Security) and Medicare withholding.
- GAs and TAs in the Academic Year classifications (code 2355 and 2354) first must be separated at the end of their AY appointment, and then appointed via an A52 transaction to the Monthly classification (code 2325 and 2353) at the beginning of the break/summer term. Retirement Account Code (PIMS Item 505) must be set to “TM” to trigger DPA PST (in lieu of Social Security) and Medicare withholding.
- If a continuing appointment expires during the break/summer term but a new appointment is made, the campus must post a new A52 transaction with Retirement Account Code (PIMS Item 505) set to “TM” for the duration of the break/summer term, until such time that the student appointment qualifies for student FICA exemption. If the student’s appointment expiration date has not expired but the student is subject to DPA PST and Medicare withholding, process a 505 transaction with Retirement Account Code (PIMS Item 505) set to “TM.”

TABLE 1.—ESTIMATED ANNUAL REPORTING BURDEN<sup>1</sup>

21 CFR Section	No. of Respondents	Annual Frequency per Response	Total Annual Responses	Hours per Response	Total Hours	Total Operating and Maintenance Costs
179.21(a)(5), (b)(1)(iv), and (b)(2)(v)	1	1	1	1	1	\$100

<sup>1</sup>There are no capital costs associated with this collection of information.

*Estimated Annualized Cost for the Burden Hours*

The operating and maintenance cost associated with this collection is \$100 for preparation of labels.

The information collection requirements in this final rule have been approved under OMB control number 0910-0549. This approval expires January 31, 2005. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

**VII. Objections**

Any person who will be adversely affected by this regulation may file with the Division of Dockets Management (see ADDRESSES) written or electronic objections. Each objection shall be separately numbered, and each numbered objection shall specify with particularity the provisions of the regulation to which objection is made and the grounds for the objection. Each numbered objection on which a hearing is requested shall specifically so state. Failure to request a hearing for any particular objection shall constitute a waiver of the right to a hearing on that objection. Each numbered objection for which a hearing is requested shall include a detailed description and analysis of the specific factual information intended to be presented in support of the objection in the event that a hearing is held. Failure to include such a description and analysis for any particular objection shall constitute a waiver of the right to a hearing on the objection. Three copies of all documents are to be submitted and are to be identified with the docket number found in brackets in the heading of this document. Any objections received in response to the regulation may be seen in the Division of Dockets Management between 9 a.m. and 4 p.m., Monday through Friday.

**VIII. References**

The following references have been placed on display in the Division of Dockets Management and may be seen by interested persons between 9 a.m. and 4 p.m., Monday through Friday.

1. Findlay, D. J. S., R. A. Forrest, and G. M. Smith, "Neutron-Induced Activation of Food," (Harwell Report), AEA-InTec-1051, 1992.
2. Ryge, P., I. Bar-Nir, M. Simic, "Food Safety Effects of Inspection by SAIC Pulsed Fast Neutron Analysis Explosive Detection System," SAIC, 1992.
3. Easterly, C. E., K. F. Eckerman, R. H. Ross, D. M. Opresko, "Assessment of Petition to Use Pulsed Fast Neutron Analysis (PFNA) in Inspection of Shipping Containers Containing Foods," Oak Ridge National Laboratory, Life Sciences Division, 2003.

**List of Subjects in 21 CFR Part 179**

Food additives, Food labeling, Food packaging, Radiation protection, Reporting and recordkeeping requirements, Signs and symbols.

■ Therefore, under the Federal Food, Drug, and Cosmetic Act and under authority delegated to the Commissioner of Food and Drugs and redelegated to the Director, Center for Food Safety and Applied Nutrition, 21 CFR part 179 is amended as follows:

**PART 179—IRRADIATION IN THE PRODUCTION, PROCESSING AND HANDLING OF FOOD**

■ 1. The authority citation for 21 CFR part 179 continues to read as follows:

**Authority:** 21 U.S.C. 321, 342, 343, 348, 373, 374.

■ 2. Section 179.21 is amended by adding paragraphs (a)(5), (b)(1)(iv), and (b)(2)(v) to read as follows:

**§ 179.21 Sources of radiation used for inspection of food, for inspection of packaged food, and for controlling food processing.**

- \* \* \* \*
- (a) \* \* \*
- (5) Monoenergetic neutron sources producing neutrons at energies not less than 1 MeV but no greater than 14 MeV.
- (b) \* \* \*
- (1) \* \* \*
- (iv) The minimum and maximum energy of radiation emitted by neutron source.
- (2) \* \* \*
- (v) A statement that no food shall be exposed to a radiation source listed in paragraph (a)(5) of this section so as to receive a dose in excess of 0.01 gray (Gy).

Dated: December 14, 2004.

**Leslye M. Fraser,**

*Director, Office of Regulations and Policy, Center for Food Safety and Applied Nutrition.*  
[FR Doc. 04-27868 Filed 12-20-04; 8:45 am]

**BILLING CODE 4160-01-S**

**DEPARTMENT OF THE TREASURY**

**Internal Revenue Service**

**26 CFR Part 31**

[TD 9167]

**RIN 1545-BC81**

**Student FICA Exception**

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Final regulation.

**SUMMARY:** This document contains final regulations providing guidance regarding the employment tax exceptions for student services. These regulations affect schools, colleges, and universities and their employees.

**DATES:** *Effective date:* December 21, 2004.

*Applicability date:* These regulations are applicable for services performed on or after April 1, 2005.

**FOR FURTHER INFORMATION CONTACT:** John Richards of the Office of Associate Chief Counsel (Tax Exempt and Government Entities), (202) 622-6040 (not a toll-free number).

**SUPPLEMENTARY INFORMATION:**

**Background**

This document contains amendments to 26 CFR part 31 under sections 3121(b)(10) and 3306(c)(10)(B) of the Internal Revenue Code (Code). These sections except from "employment" for Federal Insurance Contributions Act (FICA) and Federal Unemployment Tax Act (FUTA) purposes, respectively, service performed in the employ of a school, college, or university by a student who is enrolled and regularly attending classes at such school, college, or university. In addition, this document contains amendments to 26 CFR part 31 under section 3121(b)(2).

This section excepts from employment for FICA purposes domestic service performed in a local college club, or local chapter of a college fraternity or sorority, by a student who is enrolled and is regularly attending classes at a school, college, or university.

Proposed regulations under sections 3121(b)(2), 3121(b)(10), and 3306(c)(10)(B) were published in the **Federal Register** on February 25, 2004 (69 FR 8604, 2004-10 I.R.B. 571).

Written and electronic comments responding to the notice of proposed rulemaking were received. A public hearing was held on June 16, 2004. After consideration of all the comments, the proposed regulations are adopted as amended by this Treasury decision. The revisions are discussed below.

### Explanation of Provisions and Summary of Comments

The final regulations provide rules for determining whether an organization is a school, college, or university (SCU) and whether an employee is a student for purposes of sections 3121(b)(10), 3121(b)(2), and 3306(c)(10)(B) of the Code. Many comments were received on the proposed regulations and several witnesses testified at the hearing which was held June 16, 2004. After consideration of the comments and testimony, the Treasury department and the IRS decided to make several significant changes described below.

#### 1. School, College, or University

The exceptions from employment for student services apply only if the employee is a student enrolled and regularly attending classes at a SCU. Under the proposed regulations, whether an organization is a SCU is determined with reference to the organization's primary function. An organization whose primary function is to carry on educational activities qualifies as a SCU for purposes of the student exceptions from employment.

A few commentators suggested that an organization, such as a teaching hospital, that has embedded within it a division or function that carries on educational activities should be treated as a SCU for purposes of the student exceptions from employment.

The final regulations retain the primary function standard as described in the proposed regulations. As discussed in the preamble to the proposed regulations, the primary function standard is based upon the existing statutory and regulatory language under section 3121(b)(10), as well as the legislative history relating to the student exception from employment under section 3121(b)(10).

#### 2. Enrolled and Regularly Attending Classes

The exceptions from employment for student services require that an employee be "enrolled and regularly attending classes" in order to have the status of a student. Under the proposed regulations, "a class is an instructional activity led by a knowledgeable *faculty member* for identified students following an established curriculum."

Commentators requested clarification regarding whether an instructional activity must be led by a regular faculty member in order to be considered a class, or whether an activity led by an adjunct faculty member, graduate teaching assistant, or other qualified individual hired to lead the activity could be considered a class.

The final regulations clarify that a class is an instructional activity led by a faculty member "or other qualified individual" following an established curriculum. Thus, an instructional activity led by an adjunct faculty member, graduate assistant, or other qualified individual can qualify as a class for purposes of the student exceptions from employment.

#### 3. Student Status

The existing student FICA regulations provide that an employee whose services are incident to and for the purpose of pursuing a course of study has the status of a student.

§ 31.3121(b)(10)-2(c). The proposed regulations provide that in order for an employee's services to be considered incident to and for the purpose of pursuing a course of study, the educational aspect of the relationship between the employee and the employer, as compared to the service aspect, must be predominant. Under the proposed regulations, if an employee is a "career employee," then the service aspect of the employee's relationship with the employer is considered predominant, and thus the employee's services are not considered incident to and for the purpose of pursuing a course of study. The proposed regulations provide that the following employees are considered career employees: (1) Employees who regularly perform services 40 hours or more per week; (2) professional employees; (3) employees who receive certain employment benefits; and (4) employees required to be licensed to work in the field in which the employees are performing services. The IRS requested comments on the criteria used to identify employees having the status of a career employee.

Commentators expressed concern about using these criteria to make

certain employees automatically ineligible for the student FICA exception. Rather, according to commentators, whether an employee's services are incident to and for the purpose of pursuing a course of study should be based upon all the relevant facts and circumstances.

The final regulations provide that the educational and service aspects of an employee's relationship with the employer are generally evaluated for an academic term based upon all the relevant facts and circumstances. Similar criteria to those identified in the proposed regulations are described in the final regulations as relevant factors, not dispositive criteria, in determining whether the educational or service aspect of an employee's relationship with the employer is predominant. Nevertheless, under the final regulations, if an employee is a "full-time employee," then the employee's services are not incident to and for the purpose of pursuing a course of study. In addition, based upon comments received, the criteria identified in the proposed regulations have been modified as described below.

#### A. Full-Time Employee and Hours Worked

The proposed regulations provide that an employee who "regularly performs services 40 hours or more per week" is a career employee, and is thus ineligible for the student exception from employment. Commentators expressed concern that the 40 hour criterion would be administratively impracticable because it would be difficult to monitor an employee's actual hours worked during an academic term. In addition, commentators expressed concern that the meaning of "regularly" is unclear, making it difficult to assess the effect of changes in hours worked from week to week. Commentators also requested clarification on whether an employee's number of hours worked during academic breaks is considered in determining whether the employee is eligible for the student FICA exception.

The final regulations modify the hours worked criterion. The final regulations provide that the services of a "full-time employee" are not incident to and for the purpose of pursuing a course of study. Under the final regulations, a full-time employee is an employee who is considered a full-time employee based upon the employer's standards and practices, except that an employee whose "normal work schedule is 40 hours or more per week" is considered a full-time employee. This standard is intended to improve administrability for employers. Whether

an employee is a full-time employee based upon the employer's standards and practices, or based upon the employee's normal work schedule, should be determinable by employers at the start of an academic term, thus reducing instances where an employee's status shifts from student to non-student during an academic term. An employee's normal work schedule does not change, for example, based upon changes in work demands that are unforeseen at the start of an academic term causing the employee to work additional hours beyond his normal work schedule. In addition, time spent performing services that have an educational or instructional aspect is considered in determining an employee's normal work schedule. Finally, the final regulations provide that an employee's work schedule during an academic break is not considered in determining whether the employee's normal work schedule is 40 hours or more per week.

The final regulations provide that if an employee does not have the status of a full-time employee, then the employee's normal work schedule and actual number of hours worked per week are relevant factors in determining whether the service aspect or educational aspect of the employee's relationship with the employer is predominant. Thus, if an employee is normally scheduled to work 20 hours per week, but consistently works more than 40 hours per week, the amount of time actually worked is taken into account in determining whether or not the employee qualifies as a student.

#### *B. Professional Employee and Licensure*

##### 1. Professional Employee

The proposed regulations provide that a "professional employee" is a career employee, and is thus ineligible for the student exception from employment. Under the proposed regulations, a professional employee is an employee who performs work: (1) Requiring knowledge of an advanced type in a field of science or learning, (2) requiring the consistent exercise of discretion and judgment, and (3) that is predominantly intellectual and varied in character.

Commentators expressed concern that the professional employee criterion would inappropriately disqualify the services of many graduate research and teaching assistants from eligibility for the student exceptions from employment. Commentators maintained that graduate research and teaching assistants are primarily students, and thus their services should not automatically be ineligible for the

student exceptions based upon the professional employee criterion.

The final regulations provide that whether an employee is a professional employee is a relevant factor, not a dispositive criterion, in evaluating the service aspect of the employee's relationship with the employer. Under the final regulations, if an employee has the status of a professional employee, then that suggests the service aspect of the employee's relationship with the employer is predominant. Whether a professional employee is a student will depend upon all the facts and circumstances. Thus, under the final regulations, those graduate assistants and other employees whose work is described under the professional employee standard are not automatically ineligible for the student exception.

##### 2. Licensure

The proposed regulations provide that an employee who is required to be licensed under state or local law to work in the field in which the employee performs services is a career employee, and is thus ineligible for the student exception. The preamble to the proposed regulations requested comments on the licensure criterion and whether this criterion should be further refined or clarified.

Commentators expressed concern that the licensure criterion under the proposed regulations is overly broad because it would cause employees licensed for health and safety reasons, such as van drivers and life guards, to be ineligible for student status.

Under the final regulations, an employee's licensure status is not a dispositive criterion. Instead, the final regulations provide if an employee is a professional employee, then whether the employee is licensed is a relevant factor in determining whether the service aspect of the employee's relationship with the employer is predominant. The final regulations provide that if an employee has the status of a licensed, professional employee, then that fact further suggests that the service aspect of the employee's relationship with the employer is predominant. However, a worker who is a licensed, professional employee could be considered a student based upon all the relevant facts and circumstances.

#### *C. Employment Benefits*

The proposed regulations provide that an employee who is eligible to receive certain employment benefits is considered a career employee, and is thus ineligible for the student exception.

Commentators expressed concern that eligibility to receive employment benefits should not disqualify an individual from the student exception. Commentators noted that some state statutes make student employees eligible for retirement and other benefits, meaning that student employees in those states could not qualify as students under the proposed regulations. In addition, commentators noted that many colleges and universities permit student employees to make elective contributions to section 403(b) arrangements. Under the proposed regulations, offering this benefit would prohibit student employees from qualifying as students for purposes of the student exceptions from employment.

The final regulations provide that eligibility to receive employment benefits is a relevant factor, not a dispositive criterion, in determining whether the service aspect of an employee's relationship with the employer is predominant. Thus, an employee who is eligible for employment benefits can still qualify as a student for purposes of the student exceptions from employment. In addition, the final regulations provide that eligibility to receive health insurance benefits is not considered in determining whether the service aspect is predominant, and eligibility for benefits mandated by state or local law is given less weight in determining whether the service aspect is predominant.

##### 4. Effective Date

Commentators objected to the proposed effective date of February 25, 2004, asserting that it would take some time to adjust to the new rules set forth in the proposed regulations. In response to these comments, the final regulations are applicable with respect to services performed on or after April 1, 2005.

##### 5. Revenue Procedure Replacing Rev. Proc. 98-16

When the IRS issued the proposed regulations, it also issued Notice 2004-12 (2004-10 I.R.B. 556) suspending Rev. Proc. 98-16 (1998-1 C.B. 403) and proposing to replace it with a revenue procedure that is consistent with the proposed regulations. The IRS solicited comments on the proposed revenue procedure. Comments were received and considered in conjunction with the comments on the proposed regulations. The proposed revenue procedure has been modified in response to comments, and in order to provide guidance that is consistent with the final regulations, is being issued in final form in Rev. Proc.

2005–11 (to be published in I.R.B. 2005–2) modifying and superseding Rev. Proc. 98–16. Rev. Proc. 2005–11 is applicable with respect to services performed on or after April 1, 2005. Taxpayers may rely upon Rev. Proc. 98–16 with respect to services performed prior to April 1, 2005.

**Special Analyses**

It has been determined that these final regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. In addition, because no collection of information is imposed on small entities, the provisions of the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Code, the proposed regulations preceding these regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on the impact on small business.

**Drafting Information**

The principal author of these proposed regulations is John Richards of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury Department participated in their development.

**List of Subjects in 26 CFR Part 31**

Employment taxes and collection of income tax at source.

**Adoption of Amendment to the Regulations**

■ Accordingly, 26 CFR part 31 is amended as follows:

**PART 31—EMPLOYMENT TAXES**

■ **Paragraph 1.** The authority citation for part 31 continues to read in part, as follows:

**Authority:** 26 U.S.C. 7805 \* \* \*

■ **Par. 2.** In § 31.3121(b)(2)–1, paragraph (d) is revised to read as follows:

**§ 31.3121(b)(2)–1 Domestic service performed by students for certain college organizations.**

\* \* \* \* \*

(d) An organization is a *school, college, or university* within the meaning of section 3121(b)(2) if its primary function is the presentation of formal instruction, it normally

maintains a regular faculty and curriculum, and it normally has a regularly enrolled body of students in attendance at the place where its educational activities are regularly carried on. See section 170(b)(1)(A)(ii) and the regulations thereunder.

\* \* \* \* \*

■ **Par. 3.** Section 31.3121(b)(10)–2 is amended by:

- 1. Revising paragraphs (a), (b), (c) and (d).
- 2. Redesignating paragraph (e) as (g).
- 3. Adding paragraphs (e) and (f).

The revisions and additions read as follows:

**§ 31.3121(b)(10)–2 Services performed by certain students in the employ of a school, college, or university, or of a nonprofit organization auxiliary to a school, college, or university.**

(a) *General rule.* (1) Services performed in the employ of a school, college, or university within the meaning of paragraph (c) of this section (whether or not the organization is exempt from income tax) are excepted from employment, if the services are performed by a student within the meaning of paragraph (d) of this section who is enrolled and is regularly attending classes at the school, college, or university.

(2) Services performed in the employ of an organization which is—

- (i) Described in section 509(a)(3) and § 1.509(a)–4;
- (ii) Organized, and at all times thereafter operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of a school, college, or university within the meaning of paragraph (c) of this section; and

- (iii) Operated, supervised, or controlled by or in connection with the school, college, or university; are excepted from employment, if the services are performed by a student who is enrolled and regularly attending classes within the meaning of paragraph (d) of this section at the school, college, or university. The preceding sentence shall not apply to services performed in the employ of a school, college, or university of a State or a political subdivision thereof by a student referred to in section 218(c)(5) of the Social Security Act (42 U.S.C. 418(c)(5)) if such services are covered under the agreement between the Commissioner of Social Security and such State entered into pursuant to section 218 of such Act. For the definitions of “operated, supervised, or controlled by”, “supervised or controlled in connection with”, and “operated in connection

with”, see paragraphs (g), (h), and (i), respectively, of § 1.509(a)–4.

(b) *Statutory tests.* For purposes of this section, if an employee has the status of a student within the meaning of paragraph (d) of this section, the amount of remuneration for services performed by the employee, the type of services performed by the employee, and the place where the services are performed are not material. The statutory tests are:

(1) The character of the organization in the employ of which the services are performed as a school, college, or university within the meaning of paragraph (c) of this section, or as an organization described in paragraph (a)(2) of this section, and

(2) The status of the employee as a student enrolled and regularly attending classes within the meaning of paragraph (d) of this section at the school, college, or university within the meaning of paragraph (c) of this section by which the employee is employed or with which the employee’s employer is affiliated within the meaning of paragraph (a)(2) of this section.

(c) *School, College, or University.* An organization is a *school, college, or university* within the meaning of section 3121(b)(10) if its primary function is the presentation of formal instruction, it normally maintains a regular faculty and curriculum, and it normally has a regularly enrolled body of students in attendance at the place where its educational activities are regularly carried on. See section 170(b)(1)(A)(ii) and the regulations thereunder.

(d) *Student Status—general rule.* Whether an employee has the status of a student performing the services shall be determined based on the relationship of the employee with the organization employing the employee. In order to have the status of a student, the employee must perform services in the employ of a school, college, or university within the meaning of paragraph (c) of this section at which the employee is enrolled and regularly attending classes in pursuit of a course of study within the meaning of paragraphs (d)(1) and (2) of this section. In addition, the employee’s services must be incident to and for the purpose of pursuing a course of study within the meaning of paragraph (d)(3) of this section at such school, college, or university. An employee who performs services in the employ of an affiliated organization within the meaning of paragraph (a)(2) of this section must be enrolled and regularly attending classes at the affiliated school, college, or university within the meaning of paragraph (c) of this section in pursuit

of a course of study within the meaning of paragraphs (d)(1) and (2) of this section. In addition, the employee's services must be incident to and for the purpose of pursuing a course of study within the meaning of paragraph (d)(3) of this section at such school, college, or university.

(1) *Enrolled and regularly attending classes.* An employee must be enrolled and regularly attending classes at a school, college, or university within the meaning of paragraph (c) of this section at which the employee is employed to have the status of a student within the meaning of section 3121(b)(10). An employee is enrolled within the meaning of section 3121(b)(10) if the employee is registered for a course or courses creditable toward an educational credential described in paragraph (d)(2) of this section. In addition, the employee must be regularly attending classes to have the status of a student. For purposes of this paragraph (d)(1), a class is an instructional activity led by a faculty member or other qualified individual hired by the school, college, or university within the meaning of paragraph (c) of this section for identified students following an established curriculum. Traditional classroom activities are not the sole means of satisfying this requirement. For example, research activities under the supervision of a faculty advisor necessary to complete the requirements for a Ph.D. degree may constitute classes within the meaning of section 3121(b)(10). The frequency of these and similar activities determines whether an employee may be considered to be regularly attending classes.

(2) *Course of study.* An employee must be pursuing a course of study in order to have the status of a student. A course of study is one or more courses the completion of which fulfills the requirements necessary to receive an educational credential granted by a school, college, or university within the meaning of paragraph (c) of this section. For purposes of this paragraph, an educational credential is a degree, certificate, or other recognized educational credential granted by an organization described in paragraph (c) of this section. A course of study also includes one or more courses at a school, college or university within the meaning of paragraph (c) of this section the completion of which fulfills the requirements necessary for the employee to sit for an examination required to receive certification by a recognized organization in a field.

(3) *Incident to and for the purpose of pursuing a course of study.* (i) *General*

*rule.* An employee's services must be incident to and for the purpose of pursuing a course of study in order for the employee to have the status of a student. Whether an employee's services are incident to and for the purpose of pursuing a course of study shall be determined on the basis of the relationship of the employee with the organization for which such services are performed as an employee. The educational aspect of the relationship between the employer and the employee, as compared to the service aspect of the relationship, must be predominant in order for the employee's services to be incident to and for the purpose of pursuing a course of study. The educational aspect of the relationship is evaluated based on all the relevant facts and circumstances related to the educational aspect of the relationship. The service aspect of the relationship is evaluated based on all the relevant facts and circumstances related to the employee's employment. The evaluation of the service aspect of the relationship is not affected by the fact that the services performed by the employee may have an educational, instructional, or training aspect. Except as provided in paragraph (d)(3)(iii) of this section, whether the educational aspect or the service aspect of an employee's relationship with the employer is predominant is determined by considering all the relevant facts and circumstances. Relevant factors in evaluating the educational and service aspects of an employee's relationship with the employer are described in paragraphs (d)(3)(iv) and (v) of this section respectively. There may be facts and circumstances that are relevant in evaluating the educational and service aspects of the relationship in addition to those described in paragraphs (d)(3)(iv) and (v) of this section.

(ii) *Student status determined with respect to each academic term.* Whether an employee's services are incident to and for the purpose of pursuing a course of study is determined separately with respect to each academic term. If the relevant facts and circumstances with respect to an employee's relationship with the employer change significantly during an academic term, whether the employee's services are incident to and for the purpose of pursuing a course of study is reevaluated with respect to services performed during the remainder of the academic term.

(iii) *Full-time employee.* The services of a full-time employee are not incident to and for the purpose of pursuing a course of study. The determination of whether an employee is a full-time employee is based on the employer's

standards and practices, except regardless of the employer's classification of the employee, an employee whose normal work schedule is 40 hours or more per week is considered a full-time employee. An employee's normal work schedule is not affected by increases in hours worked caused by work demands unforeseen at the start of an academic term. However, whether an employee is a full-time employee is reevaluated for the remainder of the academic term if the employee changes employment positions with the employer. An employee's work schedule during academic breaks is not considered in determining whether the employee's normal work schedule is 40 hours or more per week. The determination of an employee's normal work schedule is not affected by the fact that the services performed by the employee may have an educational, instructional, or training aspect.

(iv) *Evaluating educational aspect.* The educational aspect of an employee's relationship with the employer is evaluated based on all the relevant facts and circumstances related to the educational aspect of the relationship. The educational aspect of an employee's relationship with the employer is generally evaluated based on the employee's course workload. Whether an employee's course workload is sufficient in order for the employee's employment to be incident to and for the purpose of pursuing a course of study depends on the particular facts and circumstances. A relevant factor in evaluating an employee's course workload is the employee's course workload relative to a full-time course workload at the school, college or university within the meaning of paragraph (c) of this section at which the employee is enrolled and regularly attending classes.

(v) *Evaluating service aspect.* The service aspect of an employee's relationship with the employer is evaluated based on the facts and circumstances related to the employee's employment. Services of an employee with the status of a full-time employee within the meaning of paragraph (d)(3)(iii) of this section are not incident to and for the purpose of pursuing a course of study. Relevant factors in evaluating the service aspect of an employee's relationship with the employer are described in paragraphs (d)(3)(v)(A), (B), and (C) of this section.

(A) *Normal work schedule and hours worked.* If an employee is not a full-time employee within the meaning of paragraph (d)(3)(iii) of this section, then the employee's normal work schedule

and number of hours worked per week are relevant factors in evaluating the service aspect of the employee's relationship with the employer. As an employee's normal work schedule or actual number of hours worked approaches 40 hours per week, it is more likely that the service aspect of the employee's relationship with the employer is predominant. The determination of an employee's normal work schedule and actual number of hours worked is not affected by the fact that some of the services performed by the employee may have an educational, instructional, or training aspect.

(B) *Professional employee.*

(1) If an employee has the status of a professional employee, then that suggests the service aspect of the employee's relationship with the employer is predominant. A professional employee is an employee—

(i) Whose primary duty consists of the performance of work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction and study, as distinguished from a general academic education, from an apprenticeship, and from training in the performance of routine mental, manual, or physical processes;

(ii) Whose work requires the consistent exercise of discretion and judgment in its performance; and

(iii) Whose work is predominantly intellectual and varied in character (as opposed to routine mental, manual, mechanical, or physical work) and is of such character that the output produced or the result accomplished cannot be standardized in relation to a given period of time.

(2) *Licensed, professional employee.* If an employee is a licensed, professional employee, then that further suggests the service aspect of the employee's relationship with the employer is predominant. An employee is a licensed, professional employee if the employee is required to be licensed under state or local law to work in the field in which the employee performs services and the employee is a professional employee within the meaning of paragraph (d)(3)(v)(B)(1) of this section.

(C) *Employment Benefits.* Whether an employee is eligible to receive one or more employment benefits is a relevant factor in evaluating the service aspect of an employee's relationship with the employer. For example, eligibility to receive vacation, paid holiday, and paid sick leave benefits; eligibility to participate in a retirement plan or arrangement described in sections

401(a), 403(b), or 457(a); or eligibility to receive employment benefits such as reduced tuition (other than qualified tuition reduction under section 117(d)(5) provided to a teaching or research assistant who is a graduate student), or benefits under sections 79 (life insurance), 127 (qualified educational assistance), 129 (dependent care assistance programs), or 137 (adoption assistance) suggest that the service aspect of an employee's relationship with the employer is predominant. Eligibility to receive health insurance employment benefits is not considered in determining whether the service aspect of an employee's relationship with the employer is predominant. The weight to be given the fact that an employee is eligible for a particular employment benefit may vary depending on the type of benefit. For example, eligibility to participate in a retirement plan is generally more significant than eligibility to receive a dependent care employment benefit. Additional weight is given to the fact that an employee is eligible to receive an employment benefit if the benefit is generally provided by the employer to employees in positions generally held by non-students. Less weight is given to the fact that an employee is eligible to receive an employment benefit if eligibility for the benefit is mandated by state or local law.

(e) *Examples.* The following examples illustrate the principles of paragraphs (a) through (d) of this section:

*Example 1.* (i) Employee C is employed by State University T to provide services as a clerk in T's administrative offices, and is enrolled and regularly attending classes at T in pursuit of a B.S. degree in biology. C has a course workload during the academic term which constitutes a full-time course workload at T. C is considered a part-time employee by T during the academic term, and C's normal work schedule is 20 hours per week, but occasionally due to work demands unforeseen at the start of the academic term C works 40 hours or more during a week. C is compensated by hourly wages, and receives no other compensation or employment benefits.

(ii) In this *example*, C is employed by T, a school, college, or university within the meaning of paragraph (c) of this section. C is enrolled and regularly attending classes at T in pursuit of a course of study. C is not a full-time employee based on T's standards, and C's normal work schedule does not cause C to have the status of a full-time employee, even though C may occasionally work 40 hours or more during a week due to unforeseen work demands. C's part-time employment relative to C's full-time course workload indicates that the educational aspect of C's relationship with T is predominant. Additional facts supporting this conclusion are that C is not a

professional employee, and C does not receive any employment benefits. Thus, C's services are incident to and for the purpose of pursuing a course of study. Accordingly, C's services are excepted from employment under section 3121(b)(10).

*Example 2.* (i) Employee D is employed in the accounting department of University U, and is enrolled and regularly attending classes at U in pursuit of an M.B.A. degree. D has a course workload which constitutes a half-time course workload at U. D is considered a full-time employee by U under U's standards and practices.

(ii) In this *example*, D is employed by U, a school, college, or university within the meaning of paragraph (c) of this section. In addition, D is enrolled and regularly attending classes at U in pursuit of a course of study. However, because D is considered a full-time employee by U under its standards and practices, D's services are not incident to and for the purpose of pursuing a course of study. Accordingly, D's services are not excepted from employment under section 3121(b)(10).

*Example 3.* (i) The facts are the same as in Example 2, except that D is not considered a full-time employee by U, and D's normal work schedule is 32 hours per week. In addition, D's work is repetitive in nature and does not require the consistent exercise of discretion and judgment, and is not predominantly intellectual and varied in character. However, D receives vacation, sick leave, and paid holiday employment benefits, and D is eligible to participate in a retirement plan maintained by U described in section 401(a).

(ii) In this *example*, D's half-time course workload relative to D's hours worked and eligibility for employment benefits indicates that the service aspect of D's relationship with U is predominant, and thus D's services are not incident to and for the purpose of pursuing a course of study. Accordingly, D's services are not excepted from employment under section 3121(b)(10).

*Example 4.* (i) Employee E is employed by University V to provide patient care services at a teaching hospital that is an unincorporated division of V. These services are performed as part of a medical residency program in a medical specialty sponsored by V. The residency program in which E participates is accredited by the Accreditation Council for Graduate Medical Education. Upon completion of the program, E will receive a certificate of completion, and be eligible to sit for an examination required to be certified by a recognized organization in the medical specialty. E's normal work schedule, which includes services having an educational, instructional, or training aspect, is 40 hours or more per week.

(ii) In this *example*, E is employed by V, a school, college, or university within the meaning of paragraph (c) of this section. However, E's normal work schedule calls for E to perform services 40 or more hours per week. E is therefore a full-time employee, and the fact that some of E's services have an educational, instructional, or training aspect does not affect that conclusion. Thus, E's services are not incident to and for the purpose of pursuing a course of study.



Accordingly, E's services are not excepted from employment under section 3121(b)(10) and there is no need to consider other relevant factors, such as whether E is a professional employee or whether E is eligible for employment benefits.

*Example 5.* (i) Employee F is employed in the facilities management department of University W. F has a B.S. degree in engineering, and is completing the work experience required to sit for an examination to become a professional engineer eligible for licensure under state or local law. F is not attending classes at W.

(ii) In this *example*, F is employed by W, a school, college, or university within the meaning of paragraph (c) of this section. However, F is not enrolled and regularly attending classes at W in pursuit of a course of study. F's work experience required to sit for the examination is not a course of study for purposes of paragraph (d)(2) of this section. Accordingly, F's services are not excepted from employment under section 3121(b)(10).

*Example 6.* (i) Employee G is employed by Employer X as an apprentice in a skilled trade. X is a subcontractor providing services in the field in which G wishes to specialize. G is pursuing a certificate in the skilled trade from Community College C. G is performing services for X pursuant to an internship program sponsored by C under which its students gain experience, and receive credit toward a certificate in the trade.

(ii) In this *example*, G is employed by X. X is not a school, college or university within the meaning of paragraph (c) of this section. Thus, the exception from employment under section 3121(b)(10) is not available with respect to G's services for X.

*Example 7.* (i) Employee H is employed by a cosmetology school Y at which H is enrolled and regularly attending classes in pursuit of a certificate of completion. Y's primary function is to carry on educational activities to prepare its students to work in the field of cosmetology. Prior to issuing a certificate, Y requires that its students gain experience in cosmetology services by performing services for the general public on Y's premises. H is scheduled to work and in fact works significantly less than 30 hours per week. H's work does not require knowledge of an advanced type in a field of science or learning, nor is it predominantly intellectual and varied in character. H receives remuneration in the form of hourly compensation from Y for providing cosmetology services to clients of Y, and does not receive any other compensation and is not eligible for employment benefits provided by Y.

(ii) In this *example*, H is employed by Y, a school, college or university within the meaning of paragraph (c) of this section, and is enrolled and regularly attending classes at Y in pursuit of a course of study. Factors indicating the educational aspect of H's relationship with Y is predominant are that H's hours worked are significantly less than 30 per week, H is not a professional employee, and H is not eligible for employment benefits. Based on the relevant facts and circumstances, the educational aspect of H's relationship with Y is

predominant. Thus, H's services are incident to and for the purpose of pursuing a course of study. Accordingly, H's services are excepted from employment under section 3121(b)(10).

*Example 8.* (i) Employee J is a graduate teaching assistant at University Z. J is enrolled and regularly attending classes at Z in pursuit of a graduate degree. J has a course workload which constitutes a full-time course workload at Z. J's normal work schedule is 20 hours per week, but occasionally due to work demands unforeseen at the start of the academic term J works more than 40 hours during a week. J's duties include grading quizzes and exams pursuant to guidelines set forth by the professor, providing class and laboratory instruction pursuant to a lesson plan developed by the professor, and preparing laboratory equipment for demonstrations. J receives a cash stipend and employment benefits in the form of eligibility to make elective employee contributions to an arrangement described in section 403(b). In addition, J receives qualified tuition reduction benefits within the meaning of section 117(d)(5) with respect to the tuition charged for the credits earned for being a graduate teaching assistant.

(ii) In this *example*, J is employed by Z, a school, college, or university within the meaning of paragraph (c) of this section, and is enrolled and regularly attending classes at Z in pursuit of a course of study. J's full-time course workload relative to J's normal work schedule of 20 hours per week indicates that the educational aspect of J's relationship with Z is predominant. In addition, J is not a professional employee because J's work does not require the consistent exercise of discretion and judgment in its performance. On the other hand, the fact that J receives employment benefits in the form of eligibility to make elective employee contributions to an arrangement described in section 403(b) indicates that the employment aspect of J's relationship with Z is predominant. Balancing the relevant facts and circumstances, the educational aspect of J's relationship with Z is predominant. Thus, J's services are incident to and for the purpose of pursuing a course of study. Accordingly, J's services are excepted from employment under section 3121(b)(10).

(f) *Effective date.* Paragraphs (a), (b), (c), (d) and (e) of this section apply to services performed on or after April 1, 2005.

\* \* \* \* \*

■ **Par. 4.** In § 31.3306(c)(10)–2:

- 1. Paragraph (c) is revised.
  - 2. Paragraphs (d) and (e) are added.
- The revision and addition read as follows:

**§ 31.3306(c)(10)–2 Services of student in employ of a school, college, or university.**

\* \* \* \* \*

(c) *General rule.* (1) For purposes of this section, the tests are the character of the organization in the employ of which the services are performed and the status of the employee as a student

enrolled and regularly attending classes at the school, college, or university described in paragraph (c)(2) of this section, in the employ of which the employee performs the services. If an employee has the status of a student within the meaning of paragraph (d) of this section, the type of services performed by the employee, the place where the services are performed, and the amount of remuneration for services performed by the employee are not material.

(2) *School, college, or university.* An organization is a *school, college, or university* within the meaning of section 3306(c)(10)(B) if its primary function is the presentation of formal instruction, it normally maintains a regular faculty and curriculum, and it normally has a regularly enrolled body of students in attendance at the place where its educational activities are regularly carried on. See section 170(b)(1)(A)(ii) and the regulations thereunder.

(d) *Student Status—general rule.* Whether an employee has the status of a student within the meaning of section 3306(c)(10)(B) performing the services shall be determined based on the relationship of the employee with the organization for which the services are performed. In order to have the status of a student within the meaning of section 3306(c)(10)(B), the employee must perform services in the employ of a school, college, or university described in paragraph (c)(2) of this section at which the employee is enrolled and regularly attending classes in pursuit of a course of study within the meaning of paragraphs (d)(1) and (2) of this section. In addition, the employee's services must be incident to and for the purpose of pursuing a course of study at such school, college, or university within the meaning of paragraph (d)(3) of this section.

(1) *Enrolled and regularly attending classes.* An employee must be enrolled and regularly attending classes at a school, college, or university within the meaning of paragraph (c)(2) of this section at which the employee is employed to have the status of a student within the meaning of section 3306(c)(10)(B). An employee is enrolled within the meaning of section 3306(c)(10)(B) if the employee is registered for a course or courses creditable toward an educational credential described in paragraph (d)(2) of this section. In addition, the employee must be regularly attending classes to have the status of a student. For purposes of this paragraph (d)(1), a class is an instructional activity led by a faculty member or other qualified individual hired by the school, college,

or university within the meaning of paragraph (c)(2) of this section for identified students following an established curriculum. The frequency of these and similar activities determines whether an employee may be considered to be regularly attending classes.

(2) *Course of study.* An employee must be pursuing a course of study in order to have the status of a student within the meaning of section 3306(c)(10)(B). A course of study is one or more courses the completion of which fulfills the requirements necessary to receive an educational credential granted by a school, college, or university within the meaning of paragraph (c)(2) of this section. For purposes of this paragraph, an educational credential is a degree, certificate, or other recognized educational credential granted by an organization described in paragraph (c)(2) of this section. In addition, a course of study is one or more courses at a school, college or university within the meaning of paragraph (c)(2) of this section the completion of which fulfills the requirements necessary for the employee to sit for an examination required to receive certification by a recognized organization in a field.

(3) *Incident to and for the purpose of pursuing a course of study.* (i) *General rule.* An employee's services must be incident to and for the purpose of pursuing a course of study in order for the employee to have the status of a student. Whether an employee's services are incident to and for the purpose of pursuing a course of study shall be determined on the basis of the relationship of the employee with the organization for which such services are performed as an employee. The educational aspect of the relationship between the employer and the employee, as compared to the service aspect of the relationship, must be predominant in order for the employee's services to be incident to and for the purpose of pursuing a course of study. The educational aspect of the relationship is evaluated based on all the relevant facts and circumstances related to the educational aspect of the relationship. The service aspect of the relationship is evaluated based on all the relevant facts and circumstances related to the employee's employment. The evaluation of the service aspect of the relationship is not affected by the fact that the services performed by the employee may have an educational, instructional, or training aspect. Except as provided in paragraph (d)(3)(iii) of this section, whether the educational aspect or the service aspect of an

employee's relationship with the employer is predominant is determined by considering all the relevant facts and circumstances. Relevant factors in evaluating the educational and service aspects of an employee's relationship with the employer are described in paragraphs (d)(3)(iv) and (v) of this section respectively. There may be facts and circumstances that are relevant in evaluating the educational and service aspects of the relationship in addition to those described in paragraphs (d)(3)(iv) and (v) of this section.

(ii) *Student status determined with respect to each academic term.* Whether an employee's services are incident to and for the purpose of pursuing a course of study is determined separately with respect to each academic term. If the relevant facts and circumstances with respect to an employee's relationship with the employer change significantly during an academic term, whether the employee's services are incident to and for the purpose of pursuing a course of study is reevaluated with respect to services performed during the remainder of the academic term.

(iii) *Full-time employee.* The services of a full-time employee are not incident to and for the purpose of pursuing a course of study. The determination of whether an employee is a full-time employee is based on the employer's standards and practices, except regardless of the employer's reclassification of the employee, an employee whose normal work schedule is 40 hours or more per week is considered a full-time employee. An employee's normal work schedule is not affected by increases in hours worked caused by work demands unforeseen at the start of an academic term. However, whether an employee is a full-time employee is reevaluated for the remainder of the academic term if the employee changes employment positions with the employer. An employee's work schedule during academic breaks is not considered in determining whether the employee's normal work schedule is 40 hours or more per week. The determination of the employee's normal work schedule is not affected by the fact that the services performed by the individual may have an educational, instructional, or training aspect.

(iv) *Evaluating educational aspect.* The educational aspect of an employee's relationship with the employer is evaluated based on all the relevant facts and circumstances related to the educational aspect of the relationship. The educational aspect of an employee's relationship with the employer is generally evaluated based on the

employee's course workload. Whether an employee's course workload is sufficient in order for the employee's employment to be incident to and for the purpose of pursuing a course of study depends on the particular facts and circumstances. A relevant factor in evaluating an employee's course workload is the employee's course workload relative to a full-time course workload at the school, college or university within the meaning of paragraph (c)(2) of this section at which the employee is enrolled and regularly attending classes.

(v) *Evaluating service aspect.* The service aspect of an employee's relationship with the employer is evaluated based on the facts and circumstances related to the employee's employment. Services of an employee with the status of a full-time employee within the meaning of paragraph (d)(3)(iii) of this section are not incident to and for the purpose of pursuing a course of study. Relevant factors in evaluating the service aspect of an employee's relationship with the employer are described in paragraphs (d)(3)(v)(A), (B), and (C) of this section.

(A) *Normal work schedule and hours worked.* If an employee is not a full-time employee within the meaning of paragraph (d)(3)(iii) of this section, then the employee's normal work schedule and number of hours worked per week are relevant factors in evaluating the service aspect of the employee's relationship with the employer. As an employee's normal work schedule or actual number of hours worked approaches 40 hours per week, it is more likely that the service aspect of the employee's relationship with the employer is predominant. The determination of the employee's normal work schedule and actual number of hours worked is not affected by the fact that some of the services performed by the individual may have an educational, instructional, or training aspect.

(B) *Professional employee.*

(1) If an employee has the status of a professional employee, then that suggests that the service aspect of the employee's relationship with the employer is predominant. A professional employee is an employee—

(i) Whose primary duty consists of the performance of work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction and study, as distinguished from a general academic education, from an apprenticeship, and from training in the performance of routine mental, manual, or physical processes;

(ii) Whose work requires the consistent exercise of discretion and judgment in its performance; and

(iii) Whose work is predominantly intellectual and varied in character (as opposed to routine mental, manual, mechanical, or physical work) and is of such character that the output produced or the result accomplished cannot be standardized in relation to a given period of time.

(2) *Licensed, professional employee.* If an employee is a licensed, professional employee, then that further suggests the service aspect of the employee's relationship with the employer is predominant. An employee is a licensed, professional employee if the employee is required to be licensed under state or local law to work in the field in which the employee performs services and the employee is a professional employee within the meaning of paragraph (d)(3)(v)(B)(1) of this section.

(C) *Employment Benefits.* Whether an employee is eligible to receive employment benefits is a relevant factor in evaluating the service aspect of an employee's relationship with the employer. For example, eligibility to receive vacation, paid holiday, and paid sick leave benefits; eligibility to participate in a retirement plan described in section 401(a); or eligibility to receive employment benefits such as reduced tuition, or benefits under section 79 (life insurance), 127 (qualified educational assistance), 129 (dependent care assistance programs), or 137 (adoption assistance) suggest that the service aspect of an employee's relationship with the employer is predominant. Eligibility to receive health insurance employment benefits is not considered in determining whether the service aspect of an employee's relationship with the employer is predominant. The weight to be given the fact that an employee is eligible for a particular benefit may vary depending on the type of employment benefit. For example, eligibility to participate in a retirement plan is generally more significant than eligibility to receive a dependent care employment benefit. Additional weight is given to the fact that an employee is eligible to receive an employment benefit if the benefit is generally provided by the employer to employees in positions generally held by non-students.

(e) *Effective date.* Paragraphs (c) and (d) of this section apply to services performed on or after April 1, 2005.

**Mark E. Matthews,**  
*Deputy Commissioner for Services and Enforcement.*

Approved: December 15, 2004.

**Gregory F. Jenner,**  
*Acting Assistant Secretary of the Treasury.*  
[FR Doc. 04-27919 Filed 12-20-04; 8:45 am]  
BILLING CODE 4830-01-P

## DEPARTMENT OF DEFENSE

### Department of the Army

#### 32 CFR Part 503

RIN 0702-AA46

#### Apprehension and Restraint

**AGENCY:** Department of the Army, DoD.

**ACTION:** Final rule, removal.

**SUMMARY:** This action removes 32 CFR part 503 published in the **Federal Register**, March 20, 1963 (28 FR 2732). The rule is being removed because it is now obsolete.

**DATES:** Effective December 21, 2004.

**ADDRESSES:** Headquarters, Department of the Army, Office of the Provost Marshal General, ATTN: DAPM-MPD-LE, 2800 Army Pentagon, Washington, DC 20310-2800.

**FOR FURTHER INFORMATION CONTACT:** Mr. Nate Evans, (703) 693-2126.

**SUPPLEMENTARY INFORMATION:** The Office of the Provost Marshal General (DAPM-MPD-LE), is the proponent for regulations in 32 CFR part 503, and has concluded this regulation is obsolete. This regulation has been rescinded. Therefore, it would be helpful in avoiding confusion with the public if 32 CFR, part 503, is removed.

#### List of Subjects in 32 CFR Part 503

Apprehension and restraint.

#### PART 503—[REMOVED]

■ Accordingly, for reasons stated in the preamble, under the authority of Sec. 3012, 70A Stat. 157; 10 U.S.C. 3012, 32 CFR part 503, *Apprehension and Restraint*, is removed in its entirety.

**Brenda S. Bowen,**  
*Army Federal Register Liaison Officer.*  
[FR Doc. 04-22849 Filed 12-20-04; 8:45 am]  
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## DEPARTMENT OF DEFENSE

### Department of the Army

#### 32 CFR Part 630

RIN 0702-AA47

#### Absentee Deserter Apprehension Program and Surrender of Military Personnel to Civilian Authorities

**AGENCY:** Department of the Army, DoD.

**ACTION:** Final rule, removal.

**SUMMARY:** This action removes 32 CFR part 630 published in the **Federal Register** July 26, 1996 (61 FR 39073). The rule is being removed because it is now obsolete and does not affect the general public.

**DATES:** Effective December 21, 2004.

**ADDRESSES:** Headquarters, Department of the Army, Office of the Provost Marshal General, ATTN: DAPM-MPD-LE, 2800 Army Pentagon, Washington, DC 20310-2800.

**FOR FURTHER INFORMATION CONTACT:** Mr. Nate Evans, (703) 693-2126.

**SUPPLEMENTARY INFORMATION:** The Office of the Provost Marshal General (DAPM-MPD-LE), is the proponent for regulations in 32 CFR part 630, and has concluded this regulation is obsolete. This regulation has been extensively revised, and the revised regulation does not affect the general public. Therefore, it would be helpful in avoiding confusion with the public if 32 CFR part 630, is removed.

#### List of Subjects in 31 CFR Part 630

Absentee deserter apprehension program and surrender of military personnel to civilian authorities.

#### PART 630—[REMOVED]

■ Accordingly, for reasons stated in the preamble, under the authority of 10 U.S.C. 801 through 940; Manual for Courts-Martial, U.S. 2002 revised addition as amended; sec 709, Pub L. 96-154, Defense Appropriation Act. 93 Stat. 1153, 32 CFR Part 630, *Absentee Deserter Apprehension Program and Surrender of Military Personnel to Civilian Authorities*, is removed in its entirety.

**Brenda S. Bowen,**  
*Army Federal Register Liaison Officer.*  
[FR Doc. 04-27850 Filed 12-20-04; 8:45 am]  
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# Internal Revenue Service **IRS.gov**

DEPARTMENT OF THE TREASURY

## Internal Revenue Bulletin: 2005-2 January 10, 2005

### Rev. Proc. 2005-11

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#### **SECTION 1. PURPOSE**

.01 This revenue procedure sets forth generally applicable standards for determining whether services in the employ of certain public or private nonprofit schools, colleges, or universities, or affiliated organizations described in § 509(a)(3) of the Internal Revenue Code (the Code) performed by a student qualify for the exception from Federal Insurance Contributions Act (FICA) tax provided under § 3121(b)(10) of the Code (Student FICA exception). These standards are intended to provide objective and administrable guidelines for determining employment tax liability.

.02 This revenue procedure modifies the safe harbor standards provided in Rev. Proc. 98-16, 1998-1 C.B. 403, in several respects in order to align them with the recently issued final regulations under § 31.3121(b)(10)-2 of the Employment Tax Regulations (T.D. 9167, 2005-2 I.R.B. [69 F.R. 76404]).

#### **SECTION 2. BACKGROUND INFORMATION AND OVERVIEW**

.01 Proposed amendments to § 31.3121(b)(10)-2 of the Employment Tax Regulations were issued on February 25, 2004, and were proposed to be applicable with respect to services performed on or after that date (REG-156421-03, 2004-10 I.R.B. 571 [69 F.R. 8604]). Notice 2004-12, 2004-10 I.R.B. 556, issued in conjunction with the proposed amendments, proposed to replace Rev. Proc. 98-16 with a revenue procedure that is consistent with the proposed amendments. Notice 2004-12 provided interim reliance on the proposed revenue procedure as of February 25, 2004, and suspended Rev. Proc. 98-16 pending issuance of the final revenue procedure. Notice 2004-12 requested comments on the proposed revenue procedure. After consideration of the comments that were received, the proposed revenue procedure is adopted as revised by this revenue procedure, and Rev. Proc.

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98-16 is modified and superseded effective April 1, 2005.

.02 This revenue procedure modifies the safe harbor standards of Rev. Proc. 98-16 in several respects in order to align them with the final regulations. First, in order for the safe harbor to be available, in addition to being an "institution of higher education" under the Department of Education's regulations, as required by Rev. Proc. 98-16, the employer must be a school, college, or university (SCU) as defined in § 31.3121(b)(10)-2(c) of the final regulations, or an affiliated § 509(a)(3) organization with respect to the SCU. The final regulations provide that an organization is not a SCU unless its primary function is to conduct educational activities. The primary function requirement may cause the student FICA exception to be unavailable to certain organizations, such as hospitals and museums, that have embedded within them divisions or functions that carry on educational activities. See section 5 of this revenue procedure.

.03 Second, a "full-time employee" as defined in § 31.3121(b)(10)-2(d)(3)(iii) of the final regulations is ineligible for the student FICA exception. This section provides that the services of a full-time employee are not incident to and for the purpose of pursuing a course of study. Whether an employee is a full-time employee is based on the employer's standards and practices, except that an employee whose normal work schedule is 40 hours or more per week is always considered a full-time employee. Accordingly, a full-time employee is ineligible for the safe harbor provided in this revenue procedure. See section 6 of this revenue procedure.

.04 Third, the safe harbor is unavailable with respect to the services of a "professional employee" as defined in § 31.3121(b)(10)-2(d)(3)(v)(B)(1) of the final regulations. This section provides that a professional employee is an employee whose work: (1) requires knowledge of an advanced type in a field of science or learning, (2) requires the consistent exercise of discretion and judgment, and (3) is predominantly intellectual and varied in character. Although the safe harbor is unavailable, a professional employee may qualify for the student FICA exception based on consideration of all the facts and circumstances. See section 6 of this revenue procedure.

.05 Fourth, and finally, this revenue procedure expands the list of employment benefits that cause an employee to be ineligible for the safe harbor. This change is consistent with § 31.3121(b)(10)-2(d)(3)(v)(C) of the final regulations, which provides that eligibility for employment benefits generally suggests that an employee is not a student. Rev. Proc. 98-16 provides that the services of a "career employee" are ineligible for the safe harbor. Under Rev. Proc. 98-16, a career employee is an employee who is eligible to participate in certain retirement plans, eligible for reduced tuition (with certain exceptions), or otherwise classified by the employer as a career employee. The final regulations adopt the same list of employment benefits, and add to the list eligibility for several other employment benefits that are identified. Although the safe harbor is unavailable if an employee receives employment benefits described in this revenue procedure, the employee may qualify for the student FICA exception based on consideration of all the facts and circumstances. See section 6 of this revenue procedure.

.06 Both the final regulations and this revenue procedure are applicable with respect to services performed on or after April 1, 2005. This revenue procedure provides that Rev. Proc. 98-16 is no longer suspended, and employers may rely on it with respect to services performed prior to April 1, 2005, including services performed on or after February 25, 2004, and prior to April 1, 2005. Rev. Proc. 98-16 is modified and superseded with respect to services performed on or after April 1, 2005. See section 10 of this revenue procedure.

### **SECTION 3. SCOPE**

.01 Sections 6 and 7 of this revenue procedure contain generally applicable standards for determining whether services performed by employees of certain institutions of higher education are eligible for the student FICA exception.

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.02 The standards contained in this revenue procedure do not apply to employees who are postdoctoral students, postdoctoral fellows, medical residents, or medical interns because the services performed by these employees cannot be assumed to be incident to and for the purpose of pursuing a course of study. The employment activities of these individuals overlap with the activities arguably comprising a course of study, and thus it is not appropriate to apply the standards of this revenue procedure to these individuals.

.03 The standards contained in this revenue procedure may not constitute the exclusive method for determining whether the student FICA exception applies. If the standard for qualifying for the exclusion described in section 7 of this revenue procedure (providing generally that an employee enrolled at least half-time at an institution of higher education has the status of student) is not met, whether or not services in the employ of a SCU, or an affiliated § 509(a)(3) organization qualify for the student FICA exception will depend on consideration of all the facts and circumstances.

#### **SECTION 4. BACKGROUND LAW**

.01 Sections 3101 and 3111 of the Code impose social security and Medicare taxes (FICA taxes) on employees and employers, respectively, equal to a percentage of the wages received by an individual with respect to employment.

.02 Section 3121(a) of the Code defines "wages" for purposes of FICA taxes as all remuneration for employment, with certain exceptions. Section 3121(b) of the Code defines "employment" as services performed by an employee for an employer, with certain exceptions.

.03 Section 3121(b)(10) of the Code excepts from the definition of employment services performed in the employ of a SCU (whether or not that organization is exempt from income tax), or an affiliated § 509(a)(3) organization if the services are performed by a student who is enrolled and regularly attending classes at that SCU. Remuneration for services excluded from the definition of employment under § 3121(b)(10) of the Code is not subject to FICA taxes.

.04 Section 31.3121(b)(10)-2(b) of the final Employment Tax Regulations provides that the tests for determining eligibility for the student FICA exception are (1) whether the employer is a SCU within the meaning of § 31.3121(b)(10)-2(c) of the final regulations, and (2) whether the employee is a student within the meaning of § 31.3121(b)(10)-2(d) of the final regulations. If the employee has the status of a student, the amount of remuneration for services performed by the employee, the type of services performed by the employee, and the place where the services are performed are immaterial for purposes of the student FICA exception.

.05 Section 31.3121(b)(10)-2(c) of the final regulations provides that an organization is a SCU within the meaning of § 3121(b)(10) if its primary function is the presentation of formal instruction, it normally maintains a regular faculty and curriculum, and it normally has a regularly enrolled body of students in attendance at the place where its educational activities are regularly carried on.

.06 Section 31.3121(b)(10)-2(d)(3)(i) of the final regulations provides that in order to have the status of a student, an employee's services for the SCU must be incident to and for the purpose of pursuing a course of study at the SCU. Whether an employee's services are incident to and for the purpose of pursuing a course of study is determined on the basis of the relationship of the employee with the organization for which such services are performed as an employee. The educational aspect of the relationship, as compared to the service aspect, must be predominant in order for the employee's services to be incident to and for the purpose of pursuing a course of study. Except in the case of a full-time employee described in § 31.3121(b)(10)-2(d)(3)(iii) of the final regulations, whether the educational aspect or service aspect of an employee's relationship with the employer is predominant is determined by considering all the relevant facts and circumstances. Whether an employee's

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services are incident to and for the purpose of pursuing a course of study is determined separately with respect to each academic term. Relevant factors in evaluating the educational and service aspects of an employee's relationship with the employer are described in §§ 31.3121(b)(10)-2(d)(3)(iv) and (v) of the final regulations respectively.

.07 Section 31.3121(b)(10)-2(d)(3)(iii) of the final regulations provides that the services of a full-time employee are not incident to and for the purpose of pursuing a course of study. The determination of whether an employee is a full-time employee is based on the employer's standards and practices, except regardless of the employer's classification of the employee, an employee whose normal work schedule is 40 hours or more per week is considered a full-time employee. The employee's work schedule during academic breaks is not considered in determining whether the employee's normal work schedule is 40 hours or more per week.

.08 Section 31.3121(b)(10)-2(d)(3)(iv) of the final regulations provides that the educational aspect of an employee's relationship with the employer is generally evaluated based on the employee's course workload. Whether an employee's course workload is sufficient in order for the employee's employment to be incident to and for the purpose of pursuing a course of study depends on the particular facts and circumstances. A relevant factor in evaluating an employee's course workload is the employee's course workload relative to a full-time course workload at the SCU at which the employee is enrolled and regularly attending classes.

.09 Section 31.3121(b)(10)-2(d)(3)(v) of the final regulations provides certain relevant factors in evaluating the service aspect of an employee's relationship with the employer. Under § 31.3121(b)(10)-2(d)(3)(v)(B)(1), if an employee has the status of a professional employee, then that suggests the service aspect of the employee's relationship with the employer is predominant. A professional employee is an employee—

(1) Whose primary duty consists of the performance of work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction and study, as distinguished from a general academic education, from an apprenticeship, and from training in the performance of routine mental, manual, or physical processes;

(2) Whose work requires the consistent exercise of discretion and judgment in its performance; and

(3) Whose work is predominantly intellectual and varied in character (as opposed to routine mental, manual, mechanical, or physical work) and is of such character that the output produced or the result accomplished cannot be standardized in relation to a given period of time.

.10 Section 31.3121(b)(10)-2(d)(3)(v)(C) of the final regulations provides that whether an employee is eligible to receive employment benefits is a relevant factor in evaluating the service aspect of an employee's relationship with the employer. However, eligibility for benefits mandated by law is given a lesser amount of weight in evaluating the relationship.

.11 Section 218 of the Social Security Act (the Act), 42 U.S.C. section 418, requires the Commissioner of Social Security, if requested by a State, to enter into an agreement with the State to provide Social Security coverage for services performed by individuals as employees of such State. The State may request that the coverage agreement exclude from coverage service performed by a student. If a State has exercised its option under § 218 of the Act to provide coverage for its employees, and has not chosen to exclude students from such coverage, § 3121(b)(10) of the Code provides that the services of students will not qualify for the student FICA exception; that is, the students' services will be covered and the wages will be subject to FICA taxation.

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## **SECTION 5. SAFE HARBOR APPLIES TO CERTAIN INSTITUTIONS OF HIGHER EDUCATION**

.01 The standards contained in this revenue procedure apply to an "institution of higher education" meeting the requirements of § 31.3121(b)(10)-2(c) of the final regulations. For purposes of this revenue procedure, the term "institution of higher education" means any public or private nonprofit SCU within the meaning of § 31.3121(b)(10)-2(c), or affiliated § 509(a)(3) organization with respect to the SCU, that meets the requirements set forth in Department of Education regulations at 34 C.F.R. § 600.4, as amended from time to time, and that is accredited or preaccredited by a nationally recognized accrediting agency as defined in the Department of Education regulations at 34 C.F.R. § 600.2.

.02 Services for other institutions may also be eligible for the student FICA exception. Thus, for example, services performed by a student for a secondary school may be eligible for the student FICA exception. Whether or not services for other institutions, such as secondary schools, qualify for the student FICA exception is determined based on the facts and circumstances of each case.

## **SECTION 6. SAFE HARBOR NOT AVAILABLE FOR CERTAIN EMPLOYEES**

.01 Services performed by an employee with the status of a "full-time employee" within the meaning of § 31.3121(b)(10)-2(d)(3)(iii) of the final regulations are not eligible for the student FICA exception because such services are not incident to and for the purpose of pursuing a course of study. Accordingly, the services of a full-time employee are not eligible for the safe harbor provided under section 7 of this revenue procedure.

.02 Services performed by a "professional employee" within the meaning of § 31.3121(b)(10)-2(d)(3)(v)(B)(1) of the final regulations are not eligible for the safe harbor provided under section 7 of this revenue procedure, because such services cannot generally be considered to be incident to and for the purpose of pursuing a course of study. However, the services of a professional employee may be eligible for the student FICA exception based on consideration of all the facts and circumstances.

.03 Services performed by an employee who receives or is eligible to receive employment benefits as described in this paragraph 6.03 (except as provided in paragraph 6.04 of this revenue procedure) are not eligible for the safe harbor provided under section 7 of this revenue procedure, because such services cannot generally be considered to be incident to and for the purpose of pursuing a course of study. However, the services of an employee who receives or is eligible for employment benefits as described in this paragraph 6.03 may be eligible for the student FICA exception based on consideration of all the facts and circumstances. For purposes of this revenue procedure, an employee's services are not eligible for the safe harbor provided under section 7 of this revenue procedure if the individual —

- (1) Is eligible for vacation, sick leave, or paid holiday benefits;
- (2) Is eligible to participate in any retirement plan described in § 401(a) of the Code that is established or maintained by the institution, or would be eligible to participate if age and service requirements were met;
- (3) Is eligible to receive an allocation of employer contributions other than contributions described in § 402(g) of the Code under an arrangement described in § 403(b) of the Code, or would be eligible to receive such allocations if age and service requirements were met, or if contributions described in § 402(g) of the Code were made by the employee;
- (4) Is eligible to receive an annual deferral by nonelective employer contributions



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under an eligible deferred compensation plan described in § 457(b), or would be eligible for such annual deferrals if plan requirements were met, or if contributions by salary reduction were made by the employee to a plan described in § 457(b);

(5) Is eligible for reduced tuition (other than qualified tuition reduction under § 117(d) (5) of the Code provided to a teaching or research assistant who is a graduate student as described in section 8.03 of this revenue procedure) because of the individual's employment relationship with the institution; or

(6) Is eligible to receive one or more of the employment benefits described under sections 79 (life insurance), 127 (qualified educational assistance), 129 (dependent care assistance programs), and 137 (adoption assistance) because of the individual's employment relationship with the institution.

.04 Receipt of or eligibility for an employment benefit as described in paragraph 6.03 of this revenue procedure that is mandated by state or local law will not cause an employee to be ineligible for the safe harbor provided under section 7 of this revenue procedure.

.05 If an individual described in section 6.01, 6.02, or 6.03 of this revenue procedure performs services in multiple job positions, then the individual will with respect to any of those positions be deemed to have the same employee status with respect to all of the positions.

## **SECTION 7. STANDARDS APPLICABLE TO UNDERGRADUATE AND GRADUATE STUDENTS**

.01 An individual who is a half-time undergraduate student or a half-time graduate or professional student and who is not described in section 6.01, 6.02 or 6.03 of this revenue procedure qualifies for the student FICA exception under this revenue procedure with respect to services performed for an institution of higher education described in section 5 of this revenue procedure at which the employee is enrolled or for an affiliated § 509(a)(3) organization with respect to the institution of higher education. Services performed by a student for any other employer are not covered by the standards of this revenue procedure.

.02 An individual is deemed to be a half-time undergraduate or half-time graduate or professional student if the individual is not described in section 6.01, 6.02, or 6.03 of this revenue procedure and is an undergraduate or graduate student who is in the last semester, trimester, or quarter of a course of study requiring at least two semesters, trimesters, or quarters to complete and is enrolled in the number of credit or unit hours needed to complete the requirements for obtaining a degree, certificate, or other recognized educational credential offered by that institution of higher education even if enrolled in less than half the number required of full-time students.

.03 The determination of student status should be made at the end of the drop-add period and may be adjusted thereafter at the institution of higher education's option. The determination of student status for payroll periods ending before the end of the drop-add period may be based on the number of semester, trimester, or quarter hours being taken at the end of the registration period for that semester, trimester, or quarter.

.04 If an individual is described in section 7.01 or 7.02 of this revenue procedure, then all services performed during all payroll periods of a month or less that fall wholly or partially within the academic term are excepted from employment under the student FICA exception.

.05 The student FICA exception does not apply to services performed by an individual who is not enrolled in classes during school breaks of more than five weeks (including summer breaks of more than five weeks), other than services described in section 7.04. See Rev. Rul. 72-142, 1972-1 C.B. 317, and Rev. Rul. 74-109, 1974-1

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C.B. 288. However, the student FICA exception applies to employment which continues during normal school breaks of 5 weeks or less during which the individual is not eligible for the student FICA exception pursuant to section 7.01 of this revenue procedure provided that the individual qualifies for the student FICA exception pursuant to section 7.01 of this revenue procedure on the last day of classes or examinations preceding the break and is eligible to enroll in classes for the first academic period following the break.

.06 If the services performed by a student otherwise described in section 7.01 or 7.02 of this revenue procedure are covered under an agreement pursuant to section 218 of the Act, the student FICA exception does not apply.

.07 For provisions relating to domestic service performed by a student in a local college club, or local chapter of a college fraternity or sorority, see § 31.3121(b)(2)-1.

## **SECTION 8. DEFINITIONS**

For purposes of the standard contained in section 7 of this revenue procedure, the following definitions must be used. For purposes of the following definitions, the term "institution of higher education" means an institution of higher education as defined in section 5 of this revenue procedure.

.01 Undergraduate student. The term "undergraduate student" has the meaning attributed to that term in the Department of Education regulations at 34 C.F.R. § 674.2.

.02 Half-time undergraduate student. The term "half-time undergraduate student" has the meaning attributed to that term in the Department of Education regulations at 34 C.F.R. § 674.2.

.03 Graduate or professional student. The term "graduate or professional student" means a student who—

(1) Is enrolled at an institution of higher education for the purpose of obtaining a degree, certificate, or other recognized educational credential above the baccalaureate level or is enrolled in a program leading to a professional degree;

(2) Has completed the equivalent of at least three years of full-time study at an institution of higher education, either prior to entrance into the program or as part of the program itself; and

(3) Is not a postdoctoral student, postdoctoral fellow, medical resident, or medical intern.

.04 Half-time graduate or professional student. The term "half-time graduate or professional student" means an enrolled graduate or professional student, as defined in section 8.03 of this revenue procedure, who is carrying at least a half-time academic workload at an institution of higher education as determined by that institution under its standards and practices.

## **SECTION 9. 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 as defined in section 5 of this revenue procedure. If the standards are inappropriately applied in a manner that conflicts with this underlying purpose so as to manipulate or mischaracterize the nature of the relationship between an employee and an institution of higher education, resulting in the improper avoidance of payment of FICA taxes, then whether the student FICA exception

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applies will be determined on the basis of all the facts and circumstances (except if the employee is a full-time employee under § 31.3121(b)(10)-2(d)(3)(iii) of the final regulations), rather than on the basis of the specific standards set forth in this revenue procedure. For example, the standards would be inappropriately applied through the manipulation of the relationship between employees and the institution of higher education if a university claimed that the student FICA exception applied to research laboratory workers, who had been full-time employees within the meaning of § 31.3121(b)(10)-2(d)(3)(iii) of the regulations, but were converted to non-full-time employees 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 for many years in a job generally performed by non-students (but nonetheless was not described in section 6.01, 6.02, or 6.03 of this revenue procedure), and then enrolled at the university for six credit hours of course work per semester while continuing to work in the same job, it may be inappropriate to apply the standards of this revenue procedure to conclude that the individual's work has become incident to and for the purpose of pursuing a course of study solely because the individual enrolled for this course work. In both of these examples, whether the work is performed incident to and for the purpose of pursuing a course of study must be determined on the basis of all the relevant facts and circumstances.

## **SECTION 10. EFFECT ON OTHER PUBLISHED ITEMS**

.01 Rev. Proc. 98-16, 1998-1 C.B. 403, is no longer suspended. Employers may rely on Rev. Proc. 98-16 with respect to services performed prior to April 1, 2005.

.02 Rev. Proc. 98-16 is modified and superseded effective April 1, 2005.

## **SECTION 11. EFFECTIVE DATE**

This revenue procedure is applicable with respect to services performed on or after April 1, 2005 (the date on which T.D. 9167, 2005-2 I.R.B. [69 F.R. 76404], amending § 31.3121(b)(10)-2 is applicable).

## **SECTION 12. DRAFTING INFORMATION**

The principal author of this revenue procedure is Stephen Suetterlein of the Office of Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this revenue procedure, contact Mr. Suetterlein at (202) 622-6040 (not a toll-free call).

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## Off. of Postsecondary Educ., Education

## § 674.2

Education Act of 1958. All rights, privileges, duties, functions, and obligations existing under title II before the enactment of title IV-E continue to exist.

(2) The Secretary considers any student loan fund established under title IV-E to include the assets of an institution's student loan fund established under title II.

\*(c) Provisions in these regulations that are common to all campus-based programs are identified with an asterisk.

(d) Provisions in these regulations that refer to "loans" or "student loans" apply to all loans made under title IV-E of the HEA or title II of the National Defense Education Act.

(Authority: 20 U.S.C. 1087aa-1087hh; Pub. L. 92-318, sec. 137(d)(1))

[52 FR 45747, Dec. 1, 1987, as amended at 57 FR 32344, July 21, 1992; 59 FR 61415, Nov. 29, 1994; 64 FR 18002, Apr. 6, 2000]

## § 674.2 Definitions.

(a) The definitions of the following terms used in this part are set forth in subpart A of the Student Assistance General Provisions, 34 CFR part 668:

Academic year  
Award year  
Defense loan  
Enrolled  
Expected family contribution (EFC)  
Federal Family Education Loan (FFEL) programs  
Federal Pell Grant  
Federal Perkins loan  
Federal Perkins Loan Program  
Federal PLUS Program  
Federal SLS Program  
Federal Supplemental Educational Opportunity Grant (FSEOG) Program  
Federal Work-Study (FWS) Program  
Full-time student  
HEA  
National Defense Student Loan Program  
National Direct Student Loan (NDSL) Program  
Payment period  
Secretary

(b) The Secretary defines other terms used in this part as follows:

*Default:* The failure of a borrower to make an installment payment when due or to comply with other terms of the promissory note or written repayment agreement.

*Enter repayment:* The day following the expiration of the initial grace pe-

riod or the day the borrower waives the initial grace period. This date does not change if a forbearance, deferment, or cancellation is granted after the borrower enters repayment.

*Federal capital contribution (FCC):* Federal funds allocated or reallocated to an institution for deposit into the institution's Fund under section 462 of the HEA.

*Financial need:* The difference between a student's cost of attendance and his or her EFC.

*Fund (Federal Perkins Loan Fund):* A fund established and maintained according to § 674.8.

*Graduate or professional student:* A student who—

(1) Is enrolled in a program or course above the baccalaureate level at an institution of higher education or is enrolled in a program leading to a first professional degree;

(2) Has completed the equivalent of at least three years of full-time study at an institution of higher education, either prior to entrance into the program or as part of the program itself; and

(3) Is not receiving title IV aid as an undergraduate student for the same period of enrollment.

*Half-time graduate or professional student:* An enrolled graduate or professional student who is carrying a half-time academic workload as determined by the institution according to its own standards and practices.

*Half-time undergraduate student:* An enrolled undergraduate student who is carrying a half-time academic workload, as determined by the institution, which amounts to at least half the workload of a full-time student. However, the institution's half-time standards must equal or exceed the equivalent of one or more of the following minimum requirements:

(1) 6 semester hours or 6 quarter hours per academic term for an institution using a standard semester, trimester, or quarter system.

(2) 12 semester hours or 18 quarter hours per academic year for an institution using credit hours to measure progress, but not using a standard semester, trimester, or quarter system; or the prorated equivalent for a program of less than one year.

## §§ 674.3-674.4

## 34 CFR Ch. VI (7-1-04 Edition)

(3) 12 clock hours per week for an institution using clock hours.

(4) 12 hours of preparation per week for a student enrolled in a program of study by correspondence. Regardless of the workload, no student enrolled solely in correspondence study is considered more than half-time.

*Initial grace period:* That period which immediately follows a period of enrollment and immediately precedes the date of the first required repayment on a loan. This period is generally nine months for Federal Perkins loans, Defense loans, and NDSLs made before October 1, 1980, and six months for other Direct loans.

*Institution of higher education (institution):* A public or private nonprofit institution of higher education, a proprietary institution of higher education, or a postsecondary vocational institution.

*Institutional capital contribution (ICC):* Institutional funds contributed to establish or maintain a Fund.

*Making of a loan:* When the institution makes the first disbursement of a loan to a student for an award year.

*Master Promissory Note (MPN):* A promissory note under which the borrower may receive loans for a single award year or multiple award years.

*National credit bureau:* Any one of the national credit bureaus with which the Secretary has an agreement.

*\*Need-based employment:* Employment provided by an institution itself or by another entity to a student who has demonstrated to the institution or the entity (through standards or methods it establishes) a financial need for the earnings from that employment for the purpose of defraying educational costs of attendance for the award year for which the employment is provided.

*Post-deferment grace period:* That period of six consecutive months which immediately follows the end of certain periods of deferment and precedes the date on which the borrower is required to resume repayment on a loan.

*Satisfactory repayment arrangement:* For purposes of regaining eligibility for grant, loan, or work assistance under Title IV of the HEA, to the extent that the borrower is otherwise eligible, the making of six (6) on-time, consecutive, monthly payments on a

defaulted loan. A borrower may obtain the benefit of this paragraph with respect to renewed eligibility once on a defaulted loan.

*Student loan:* For this part means an NDSL Loan, Defense Loan, or a Federal Perkins Loan.

*Total monthly gross income:* The gross amount of income received by the borrower from employment (either full-time or part-time) and from other sources.

*Undergraduate student:* A student enrolled at an institution of higher education who is in an undergraduate course of study which usually does not exceed four academic years, or is enrolled in a four to five academic year program designed to lead to a first degree. A student enrolled in a program of any other length is considered an undergraduate student for only the first four academic years of that program.

(Authority: 20 U.S.C. 1087aa-1087hh)

[52 FR 45747, Dec. 1, 1987, as amended at 53 FR 52580, Dec. 28, 1988; 57 FR 32344, July 21, 1992; 59 FR 61404, 61415-61416, Nov. 30, 1994; 60 FR 61814, Dec. 1, 1995; 61 FR 60608, Nov. 29, 1996; 64 FR 58308, Oct. 28, 1999; 65 FR 18002, Apr. 6, 2000; 67 FR 67076, Nov. 1, 2002; 69 FR 12276, Mar. 16, 2004]

## §§ 674.3-674.4 [Reserved]

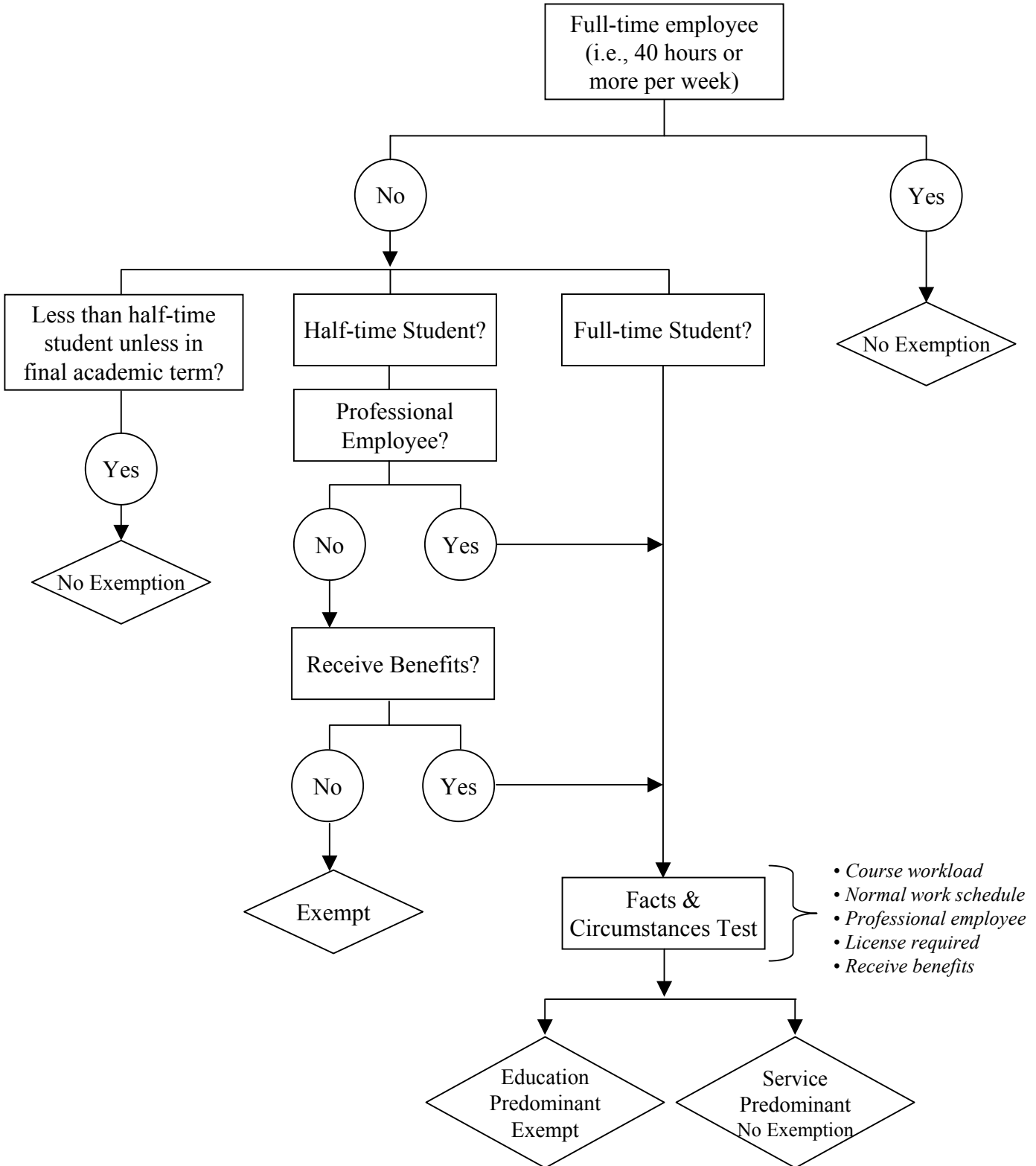
## § 674.5 Federal Perkins Loan program cohort default rate and penalties.

(a) *Default penalty.* If an institution's cohort default rate meets the following levels, a default penalty is imposed on the institution as follows:

(1) *FCC reduction.* If the institution's cohort default rate equals or exceeds 25 percent, the institution's FCC is reduced to zero.

(2) *Ineligibility.* For award year 2000-2001 and succeeding award years, an institution with a cohort default rate that equals or exceeds 50 percent for each of the three most recent years for which cohort default rate data are available is ineligible to participate in the Federal Perkins Loan Program. Following a review of that data and upon notification by the Secretary, an institution is ineligible to participate for the award year, or the remainder of

### FICA Coverage Decision Chart



## TEACHING ASSOCIATES FACTS AND CIRCUMSTANCES TEST EXAMPLES

*A fact and/or circumstance may be a relevant factor, but may not be a dispositive criterion in determining whether or not the employee qualifies for the student FICA exemption.*

### **Example One:**

Employee F is a TA enrolled and regularly attending CSU classes in pursuit of a graduate degree. F has a full-time course workload. F's normal work schedule is 10 hours per week (.25 time-base). The following criteria are considered in applying the facts and circumstances test:

- ✓ While enrolled as a full-time student, F is employed by the CSU on a limited part-time basis in the field of his advanced study.
- ✓ F does not meet the professional employee definition.
- ✓ F does not require a license to do his job.
- ✓ F does receive a very limited employee benefit package consisting of employee paid voluntary programs and some paid time off programs. F is not eligible for any health and welfare or retirement benefits.

Balancing the facts and circumstances, the educational aspect of F's relationship with the university is predominant. F's services are incident to and for the purpose of pursuing a course of study and, therefore, F's services are exempt from FICA.

### **Example Two:**

Employee I is a TA enrolled and regularly attending CSU classes in pursuit of a graduate degree. I is a half-time graduate student (course work is equal to half-time minimum) and I's normal work schedule is 16 hours per week (.40 time-base). The following criteria are considered in reviewing the "safe harbor" and later applying the facts and circumstances test:

- ✓ I is a half-time TA employed by the CSU working 16 hours per week. His work offers experience in his field of advanced study.
- ✓ I does not meet the professional employee definition.
- ✓ I does not require a license to do his job.
- ✓ I does receive a limited employee benefit package consisting of employee paid voluntary programs and some paid time off programs. I is not eligible to participate in CSU retirement, dental, vision, or life insurance programs.

This situation is not as clear cut as Example One and the decision is a close call. Since I does not meet the "safe harbor" test because he receives some employee benefits, the campus needs to perform the facts and circumstances test. Balancing the facts and circumstances, it can be determined that the educational aspect of I's relationship with the university would be considered predominant. I's services are incident to and for the purpose of pursuing his course of study. His work schedule is limited as are the benefits he receives. It appears that I would be exempt from FICA.

### **Example Three:**

Employee C is a TA enrolled and regularly attending CSU classes in pursuit of a graduate degree. C is a half-time graduate student (carrying the minimum load to be half-time) and her normal work schedule is 32 hours per week (.80 time-base). Her appointment qualifies her for enrollment in CalPERS retirement. The following criteria are considered in reviewing the "safe harbor" and later applying the facts and circumstances test:

- ✓ C is a graduate student carrying the minimum course load to be considered half-time and she is employed by the CSU working 32 hours per week (.80 timebase).
- ✓ C does not meet the professional employee definition.

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ATTACHMENT F**

- ✓ C does not require a license to do her job.
- ✓ C is eligible for a comprehensive employee benefit package that includes eligibility for CalPERS retirement.

Since C does not meet the “safe harbor” test because she receives employee benefits, the campus needs to perform the facts and circumstances test. Balancing the facts and circumstances, it appears the employment aspect of C’s relationship with the university would be considered predominant because the employee has a substantial work schedule and a comprehensive benefits package; consequently, C’s services would be subject to FICA. However, since C is eligible to participate in CalPERS retirement this employee already is required to participate in Social Security.