RESIDENT STIPENDS

Under Section 117 of the Internal Revenue Code, funds received through scholarships of fellowships in amounts not exceeding $3,600 per year for three years are excludable from a taxpayer's gross income. In determining what monies qualify as a scholarship or fellowship under this section, courts look to the Treasury Regulations for guidance. According to the Treasure Regulations, payments received by an individual will be considered a scholarship or fellowship grant if the primary purpose of the grantee's studies or research is to further the education and training of the recipient in his individual capacity and the amount provided by the grantor for such purpose does not represent compensation or payment for services.

One of the most frequently litigated issues under Section 117 is whether medical residents may exclude their stipends on the theory that the work they perform for hospitals is educational, not occupational, and that stipends are, therefore, not compensation for services rendered. Due to the unique nature of medical education, residents develop their skills through the treatment of patients which necessarily involves the performance of a service. The IRS, however, recognizes no distinction between medical residents and other on-the-job trainees who receive compensation for services. Compensation for services falls within the purview of Section 61 which defines gross income, and the IRS, therefore, views stipends as gross income and thus fully taxable.

The vast majority of judicial opinions on this issue have gone against medical residents; the courts holding that payments received by interns or residents performing services at a hospital in order to complete or receive specialized training involve a substantial quid pro quo and, therefore, represent compensation for services. Residents have prevailed in their quest to escape taxation in only a minority of cases. For example, stipends have been held to qualify for exclusion under Section 117 in situations where a resident spent only 20-25% of his time performing clinical duties and was not required to take call or maintain regular hours at the hospital, or where such payments were not conditioned upon job performance, residents' work was duplicated by attending staff physicians and not required for the operation of the hospital.

In sum, the struggle of medical resident to qualify for the exclusion under Section 117 is perhaps best summed up by an opinion of the United States Tax Court:

(o)nly rarely have the taxpayer-doctors been able to convince the courts that they qualify for the exclusion; but hope seems to spring eternal and the doctors continue to come to court with the argument that the facts and circumstances involved in the their cases are sufficiently distinguishable from the prior cases to justify the exclusion.

Thomas W. Phillips, 35 T.C.M. 293, 294-95 (1976)