

No. 14-893

In the Supreme Court of the United States

UNIVERSITY OF TEXAS SYSTEM, ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

*ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT*

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether medical residents who worked full-time at petitioners' medical centers qualified as students exempt from taxation under the Federal Insurance Contributions Act, 26 U.S.C. 3101 *et seq.*

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-18a) is reported at 759 F.3d 437. The opinion of the district court (Pet. App. 19a-42a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on July 16, 2014. A petition for rehearing was denied on October 24, 2014 (Pet. App. 43a-44a). The petition for a writ of certiorari was filed on January 21, 2015. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. a. The Federal Insurance Contributions Act (FICA), 26 U.S.C. 3101 *et seq.*, requires employers and employees to pay taxes on “wages” from “employment” in order to fund the benefits available un-

der the Social Security Act, 42 U.S.C. 401 *et seq.* See 26 U.S.C. 3101(a) and (b), 3111(a) and (b); *United States v. Quality Stores, Inc.*, 134 S. Ct. 1395, 1399 (2014); *Mayo Found. for Med. Educ. & Research v. United States*, 562 U.S. 44, 48 (2011). FICA’s definition of “employment” has a “broad reach, extending to ‘any service, of whatever nature, performed . . . by an employee for the person employing him.’” *Mayo Found.*, 562 U.S. at 48 (quoting 26 U.S.C. 3121(b)). The taxation of employment-related earnings under FICA generally corresponds with the wage-earner’s accrual of credits that increase the amount of Social Security benefits to which he is entitled. See 20 C.F.R. 404.1001; *Quality Stores*, 134 S. Ct. at 1399-1400; *United States v. Cleveland Indians Baseball Co.*, 532 U.S. 200, 212-213 (2001); *United States v. Silk*, 331 U.S. 704, 711 (1947).

FICA’s broad definition of “employment” is subject to certain limited exceptions, including an exception for service performed in the employ of a “school, college, or university” if “such service is performed by a student who is enrolled and regularly attending classes at such school, college, or university.” 26 U.S.C. 3121(b)(10). Treasury regulations have long interpreted the student exception as limited to individuals who are predominantly students and only secondarily or incidentally employees. See 16 Fed. Reg. 12,474 (Dec. 12, 1951) (promulgating 26 C.F.R. 408.219 (Cum. Supp. 1952)); 26 C.F.R. 31.3121(b)(10)-2(d). Effective April 1, 2005, an amendment to the Treasury regulations clarified that individuals who normally work 40 or more hours per week for a school, college, or university are not “students” eligible for the exemption.

26 C.F.R. 31.3121(b)(10)-2(d)(3)(iii); see 26 C.F.R. 31.3121(b)(10)-2(f).

In *Mayo Foundation, supra*, a state university and a private clinic challenged that full-time-employment rule. They asserted that full-time-employee medical residents (medical-school graduates receiving continued vocational training that involves being paid to provide medical care) should be treated as students exempt from FICA taxes. 562 U.S. at 47-51. The Court rejected that contention, holding that the full-time-employment rule was a valid exercise of agency rulemaking authority under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), and that such medical residents are subject to FICA tax. *Mayo Found.*, 562 U.S. at 52-60.

b. The Social Security Act, in setting forth the rules for accrual of work credits that govern benefits eligibility, “contains a corresponding student exception materially identical to” FICA’s. *Mayo Found.*, 562 U.S. at 49. Under 42 U.S.C. 410(a)(10), service performed in the employ of a “school, college, or university” does not count for purposes of benefits eligibility if “such service is performed by a student who is enrolled and regularly attending classes at such school, college, or university.”

As the Court observed in *Mayo Foundation*, the Social Security Administration (SSA) has “always held that resident physicians are not students.” 562 U.S. at 49 (quoting SSR 78-3, at 55-56 (S.S.R. Cum. Ed. 1978)). Since 1951, the SSA’s regulations interpreting the Social Security Act’s student exception have interpreted the Section 410(a)(10) exception as limited to individuals who are predominantly students and whose employment is only incidental to their academic

studies. See 16 Fed. Reg. 13,070 (Dec. 28, 1951) (promulgating 20 C.F.R. 404.1019 (Cum. Supp. 1952) (limitation identical to limitation in Treasury regulations)); 45 Fed. Reg. 20,074, 20,082-20,083 (Mar. 27, 1980) (revising language of limitation, now codified at 20 C.F.R. 404.1028, for stylistic purposes). In 1978, the SSA issued an interpretive ruling that expressed the agency's longstanding view that medical residents do not fall within the exception. See SSR 78-3.

2. Participation in the Social Security system is "basically mandatory." *Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment*, 477 U.S. 41, 44 (1986) (*Public Agencies*) (citation omitted). When Congress initially created the system in 1935, however, it was uncertain whether it had constitutional authority to compel the participation of state employees. *Ibid.* Accordingly, many such employees, unlike their private counterparts, are neither automatically enrolled in the Social Security system, see 42 U.S.C. 410(a)(7), nor automatically required to pay FICA taxes, 26 U.S.C. 3121(b)(7).

In 1950, in response to "pressure from States that sought Social Security coverage for their employees," Congress enacted Section 218 of the Social Security Act, 42 U.S.C. 418, which "authorizes voluntary participation by States in the Social Security System." *Public Agencies*, 477 U.S. at 44-45. Under that provision, a State may "enter into an agreement" to extend Social Security coverage to certain designated "coverage groups." 42 U.S.C. 418(a)(1) and (c)(1). Such an agreement is sometimes referred to as a "Section 218 agreement." Pet. App. 3a. A state employee's performance of service covered by a Section 218 agreement allows the employee to participate in the Social

Security system, while triggering a corresponding requirement to pay FICA taxes. 26 U.S.C. 3121(b)(7)(E).

Section 418 of Title 42 “gives States some authority over the content of the Agreements, *i.e.*, States may identify the covered employees.” *Public Agencies*, 477 U.S. at 45. To that end, the provision allows a State, if it chooses, to “exclude (in the case of any coverage group) * * * service performed by a student” from the scope of the agreement. 42 U.S.C. 418(c)(5). The provisions of a Section 218 agreement, however, must “be ‘not inconsistent with the provisions of’” 42 U.S.C. 418 itself. *Public Agencies*, 477 U.S. at 45 (quoting 42 U.S.C. 418(a)(1)). The statute provides that a particular class of services may be excepted from the agreement’s scope only if the service is also excepted from the general definition of “employment” in 42 U.S.C. 410(a). See 42 U.S.C. 418(c)(5). In other words, as relevant here, if a student’s service would necessarily be considered “employment” if performed for a private institution, a State cannot exclude such service from the scope of a Section 218 agreement; the State’s authority instead extends only to the issue of whether the student exception is available at all. *Ibid.*

3. a. Petitioners are state universities in Texas that operate medical residency programs. Pet. App. 2a, 5a. Medical residents in those programs “regularly work[] more than forty hours per week” providing medical care for patients “under the supervision of institution faculty.” *Id.* at 5a (citation omitted). They also “receive didactic lessons (including ‘teaching rounds,’ lectures and procedural workshops).” *Ibid.* Petitioners pay compensation to the medical residents for their provision of patient care. *Ibid.*

Until 2008, petitioners consistently treated the compensation paid to their medical residents as wages subject to FICA tax under Texas's Section 218 agreement. Pet. App. 5a. The Section 218 agreement itself provided that the State would pay the Treasury amounts equivalent to the taxes that would be imposed by the employment-tax provisions of the Internal Revenue Code if the services covered by the agreement constituted "employment" as defined by the Code. *Id.* at 55a. Texas's original Section 218 agreement, executed in 1951, did not exclude services performed by students. *Id.* at 4a. In 1999, Texas amended the agreement to "exclude from coverage service performed after June 30, 2000, in the employ of a school, college or university if such service is performed by a student who is enrolled and regularly attending classes" at that school, college or university. *Id.* at 5a. Even after that amendment, however, petitioners continued to withhold the employee portion, and pay the employer portion, of the FICA tax on their medical residents' wages. *Ibid.*

b. In 2008, petitioners filed administrative refund claims with the Internal Revenue Service (IRS), seeking refunds of the FICA taxes paid with respect to their medical residents in 2005. Pet. App. 5a. In 2009, after six months had elapsed without action on their refund claims, petitioners filed suit against the United States in district court to obtain the refunds. *Id.* at 6a. In those proceedings, petitioners contended for the first time that their medical residents fell within the Section 218 agreement's student exception. *Ibid.*

The district court granted summary judgment to the United States, rejecting petitioners' claims for three independent reasons. Pet. App. 19a-42a. First,

the court explained that, because the Treasury Department administers FICA, the Treasury regulation clarifying that employees who work at least 40 hours per week cannot qualify as exempt “students,” 26 C.F.R. 31.3121(b)(10)-2(d)(3)(iii), was controlling in this context. Pet. App. 30a-35a. Second, the court explained that the SSA’s regulations likewise foreclose treating the medical residents as exempt students. *Id.* at 36a-38a. Finally, the court concluded that, under standard contract-interpretation principles, the student exception in Texas’s Section 218 agreement should not be construed to encompass medical residents. *Id.* at 38a-41a.

c. The court of appeals affirmed. Pet. App. 1a-18a. Although the court observed that the parties had briefed both the regulatory issues and the contract-interpretation issue, it addressed only the latter, finding that point dispositive. *Id.* at 7a. In support of its conclusion that Section 218 agreements should be interpreted as contracts, the court of appeals relied in part on this Court’s decision in *Public Agencies, supra*, which had discussed and applied general government-contracting law in the context of Section 218 agreements. Pet. App. 10a; see *Public Agencies*, 477 U.S. at 52-53. The court also noted that, in the “primary case” on which petitioners relied, *Minnesota v. Apfel*, 151 F.3d 742 (1998), the Eighth Circuit had applied contract-interpretation principles to Minnesota’s Section 218 agreement. Pet. App. 11a; see *Apfel*, 151 F.3d at 745-747.

Applying such principles here, the court of appeals found that the parties to Texas’s Section 218 agreement (Texas and the SSA) had understood, when the agreement’s student exception was added in 1999, that

the exception would not apply to medical residents. Pet. App. 12a-18a. The court first reasoned that the student exception in Texas’s Section 218 agreement “mirrors,” and therefore “incorporate[s],” the Social Security Act’s general student exception, 42 U.S.C. 410(a)(10). Pet. App. 13a. The court then determined that by 1999, when the student exception was added to the agreement, the SSA had “clearly disclosed its understanding that medical residents did not fall within” the Social Security Act’s general student exception. *Id.* at 14a. The court found no evidence either that petitioners had a contrary understanding of the exclusion at the relevant time or that they had communicated such an understanding to the SSA. *Id.* at 15a. The court also noted that the “parties’ course of performance,” under which petitioners had paid FICA taxes consistently for eight years, provided additional “strong evidence that the parties did not intend for the student exclusion in Texas’s [Section 218] agreement to apply to [petitioners’] medical residents.” *Id.* at 16a.

ARGUMENT

Petitioners contend (Pet. 15-34) that they are not required to pay FICA taxes for the full-time work performed by their medical residents. The decision of the court of appeals is correct and consistent with *Mayo Foundation for Medical Education & Research v. United States*, 562 U.S. 44 (2011), and it does not conflict with any post-*Mayo Foundation* decision of any court of appeals. Further review is not warranted.

1. In *Mayo Foundation*, this Court held that medical residents who work at least 40 hours per week (as petitioners’ medical residents do) earn “wages” sub-

ject to taxation under FICA. 562 U.S. at 60. The Court in *Mayo Foundation* recognized that FICA exempts from taxation any compensation paid to “a student who is enrolled and regularly attending classes at [a] school, college, or university” for services “performed in the employ of” that institution. *Id.* at 49 (quoting 26 U.S.C. 3121(b)(10)). The Court concluded, however, that a Treasury regulation had permissibly construed the term “student” in that exception not to encompass employees who work at least 40 hours per week. *Id.* at 52-60; see 26 C.F.R. 31.3121(b)(10)-2(d).

Petitioners accordingly do not rely on FICA’s own student exception to support the claim that their medical residents are “students” exempt from FICA tax. They argue instead that FICA’s student exception operates differently from the corresponding exception in the Social Security Act, which provides that work performed by students does not count toward Social Security benefits eligibility. See 42 U.S.C. 410(a)(10). In particular, petitioners assert (*e.g.*, Pet. 22-23) that SSA regulations interpret the Social Security Act’s student exception to potentially *include* medical residents, even those who work at least 40 hours a week. They contend (*e.g.*, Pet. 20-22) that this asserted “regulatory framework” is incorporated into the student exception that appears in Texas’s Section 218 agreement. They argue on that basis (*e.g.*, Pet. 2) that their medical residents are not covered by Texas’s Section 218 agreement and therefore are exempt from FICA taxes. See 26 U.S.C. 3121(b)(7)(E).

Contrary to petitioners’ contention, the Social Security Act’s student exception and FICA’s student exception both treat full-time-employee medical resi-

dents the same way: such residents do not qualify as students under *either* exception. *Mayo Foundation*, 562 U.S. at 48-50, 58-60. The FICA and Social Security Act provisions that create the student exceptions are “materially identical.” *Id.* at 49. And just as a Treasury regulation now interprets FICA’s student exception not to encompass full-time medical residents, the SSA has long applied a similar regulatory interpretation to the Social Security Act’s student exception. *Ibid.* The Court in *Mayo Foundation* observed that, although the SSA has “articulated in its regulations a case-by-case approach” to whether particular individuals are students under the Social Security Act, it has “always held that resident physicians are not students.” *Ibid.* (quoting SSR 78-3, at 55-56).

The Court in *Mayo Foundation* relied on the congruence between the student exceptions in the Social Security Act and FICA to reject an argument that requiring full-time-employee medical residents to pay FICA taxes might create unfairness. 562 U.S. at 58-60. The petitioners in *Mayo Foundation* expressed concern that the Treasury regulation, which applied only to the FICA student exception, might “result in residents being taxed under FICA but denied coverage by the SSA.” *Id.* at 60. The Court explained, however, “that the SSA continues to adhere to its longstanding position that medical residents are not students.” *Ibid.* In light of that position, medical residents’ payment of FICA tax and accrual of Social Security benefits go hand-in-hand.

Under petitioners’ view of the applicable SSA regulations, medical residents employed by private institutions would pay FICA taxes without accruing corresponding work credits for purposes of Social Security

benefits. Petitioners' argument thus would introduce the very anomaly that the Court in *Mayo Foundation* disavowed. See 562 U.S. at 60. The argument is also inconsistent with Texas's Section 218 agreement, which provides that petitioners will make the payments required under the Internal Revenue Code's definition of "employment." Pet. App. 55a. It also would improperly disregard the SSA's longstanding and reasonable interpretation of its own regulatory scheme. See SSR 78-3; SSAR 98-5(8), 63 Fed. Reg. 58,446 (Oct. 30, 1998); see, e.g., *Decker v. Northwest Env'tl. Def. Ctr.*, 133 S. Ct. 1326, 1331 (2013) (recognizing that "deference is accorded to" an agency's "reasonable interpretation of its own regulation"). And, contrary to petitioners' contention (Pet. 24-25 & n.6), pre-*Mayo Foundation* circuit decisions addressing the now-defunct version of the Treasury regulations do not cast doubt on the SSA's interpretation of its own Social Security regulations, on which the Court in *Mayo Foundation* relied.

2. The SSA's longstanding interpretation of the Social Security Act's student exception provides two independent grounds supporting the result below.

First, because it has been clear at all relevant times that the SSA interprets the student exception to exclude full-time-employee medical residents, that understanding informs the interpretation of the student exception that appears in Texas's Section 218 agreement. See Pet. App. 14a-15a. Petitioners recognize that the Section 218 agreement should be interpreted in light of the "regulatory context." *E.g.*, Pet. 19, 22. As discussed above, that "regulatory context" includes the SSA's consistent position that medical residents do not qualify for the student exception.

Second, if the Section 218 agreement's student exception were interpreted to include medical residents, that aspect of the agreement would be invalid. Pursuant to 42 U.S.C. 418(c)(5), and subject only to exceptions not relevant here, a Section 218 agreement may exclude "service performed by a student" only to the extent such service "is excluded" from the general definition of "employment" in Section 410(a). Under the SSA's longstanding view that Section 410(a) does not except full-time-employee medical residents from participation in the Social Security system, such residents cannot be excepted from the scope of a Section 218 agreement.

3. Petitioners contend (Pet. 16-19) that this Court's review is warranted to resolve a conflict between the decision below and the Eighth Circuit's decision in *Minnesota v. Apfel*, 151 F.3d 742 (1998). That contention lacks merit.

a. In *Apfel*, the State of Minnesota challenged the assessment of FICA taxes on the earnings of medical residents at the University of Minnesota. 151 F.3d at 743. The Eighth Circuit applied contract-interpretation principles to Minnesota's Section 218 agreement and concluded that in 1958, when Minnesota and the SSA amended the Section 218 agreement to cover "employees" of the University of Minnesota, they "did not contemplate extending coverage to residents." *Id.* at 745-747. *Apfel's* contract-law approach to interpreting a Section 218 agreement is consistent with the approach taken by the court of appeals here, which relied on *Apfel*. Pet. App. 11a & n.4. The different results in the two cases simply reflect the different circumstances under which the relevant provision of each Section 218 agreement was adopted and

in which the intent of the parties was formed. See *id.* at 16a n.8 (distinguishing *Apfel*); compare *Apfel*, 151 F.3d at 745 & n.7, with Pet. App. 12a-15a; see *id.* at 16a-17a (noting differences in the course of performance in both cases).

As the court below recognized, the relevant contract provision in *Apfel* was adopted in 1958, while the relevant contract provision here was adopted more than four decades later. Pet. App. 16a n.8. The 1978 and 1998 SSA guidance documents on which the court below relied did not exist when the contract provision at issue in *Apfel* was incorporated into Minnesota's Section 218 agreement. Indeed, the 1998 guidance was a response to *Apfel* itself. See *id.* at 14a-15a (citing SSAR 98-5(8)).

b. The Eighth Circuit in *Apfel* also concluded, in the alternative, that “even if medical residents were considered ‘employees’ under the terms of the 1958 modification,” they still were not covered by Minnesota’s Section 218 agreement. 151 F.3d at 747-748. The Eighth Circuit noted that the 1958 modification included an express exception for students, and it believed that the exception could apply to medical residents. *Ibid.*; see *id.* at 744. The Eighth Circuit construed the 1958 student exception to be congruent with the statutory exception in 42 U.S.C. 410(a)(10); it understood SSA regulations to require a case-by-case approach to determining whether a particular individual qualified for the Section 410(a)(10) exclusion; and it believed that a categorical conclusion that full-time medical residents are not students was inconsistent with those regulations. *Apfel*, 151 F.3d at 747-748 (citing 20 C.F.R. 404.1028(c) and SSR 78-3).

Petitioners suggest (Pet. 16-19) that *Apfel*'s view of the regulatory framework, if applied here, would require interpreting the student exception in Texas's Section 218 agreement to cover their medical residents. The Eighth Circuit itself, however, has not applied *Apfel* in that manner. In a subsequent decision that this Court eventually affirmed in *Mayo Foundation*, the Eighth Circuit again addressed a claim that medical residents employed by the University of Minnesota were exempt from FICA tax. *Mayo Found. for Med. Educ. & Research v. United States*, 568 F.3d 675, 676 (2009), *aff'd*, 562 U.S. 44 (2011). Focusing on the post-*Apfel* Treasury regulation that classified full-time medical residents as non-student employees, the Eighth Circuit held that "the residents' compensation for health care and patient services was subject to FICA taxes." *Id.* at 683.

The Eighth Circuit's conclusion in *Mayo Foundation* accords fully with the court of appeals' conclusion here that medical residents employed by the University of Texas are likewise subject to FICA taxes. Although the Eighth Circuit did not expressly reconcile the conclusion it reached in *Mayo Foundation* with the conclusion it had reached in *Apfel*, the decision in *Mayo Foundation* at the very least creates substantial doubt that the outcome here would have been different if this case had arisen in the Eighth Circuit. That is particularly so in light of this Court's decision affirming the Eighth Circuit's judgment in *Mayo Foundation*.

4. Petitioners contend (Pet. 32-34) that the court of appeals' decision conflicts with the principle that a taxpayer is entitled to pay a tax and later seek a refund. No such conflict exists, and petitioners' reliance

(Pet. 33) on *Reich v. Collins*, 513 U.S. 106 (1994), is misplaced.

In *Reich*, a State “held out what plainly appeared to be a ‘clear and certain’ postdeprivation remedy * * * and then declared, only after Reich and others had paid the disputed taxes, that no such remedy exist[ed].” 513 U.S. at 111. Here, however, petitioners could and did avail themselves of a postdeprivation remedy by bringing a suit to recover the FICA taxes that they had previously paid. Unlike the plaintiffs in *Reich*, petitioners’ previous payment of those taxes did not deny them access to a remedial scheme. It was instead one factor the court below considered in adjudicating the merits of their tax-refund claim. The court appropriately recognized that the parties’ long-standing course of performance under Texas’s Section 218 agreement reflected their recognition that the agreement includes full-time-employee medical residents within the Social Security system. Pet. App. 16a.

Petitioners identify no decision holding that such a course of performance is irrelevant in interpreting a Section 218 agreement. Indeed, the Eighth Circuit in *Apfel* likewise relied on the parties’ course of performance—there, the consistent *nonpayment* of taxes on medical residents’ earnings—as one factor bearing on the proper interpretation of the Section 218 agreement at issue in that case. See Pet. App. 16a-17a (citing *Apfel*, 151 F.3d at 745 n.7). Particularly because the SSA regulations themselves would support the court of appeals’ decision without regard to course of performance or any other contract-interpretation principles, see p. 11, *supra*, further review is not warranted.

CONCLUSION

The petition for a writ of certiorari should be denied.
Respectfully submitted.

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MARCH 2015