

Tips on Tips



A Guide to
Tip Income Reporting
**for Employers in the
Food and Beverage Industry**



**If you are an employer in
the food and beverage industry,
this guide is for you.**

The Internal Revenue Service (IRS) began its *Tip Rate Determination/Education Program (TRD/EP)* in October 1993 for the food and beverage industry. The objective of the Program has been to improve and ensure compliance by employers and employees with statutory provisions relating to tip income.

The Program of Tip Reporting

What tip reporting options are available?

- *Tip Rate Determination Agreement (TRDA)*
- *Tip Reporting Alternative Commitment (TRAC)*
- Institute your own reporting system to comply with the tax law

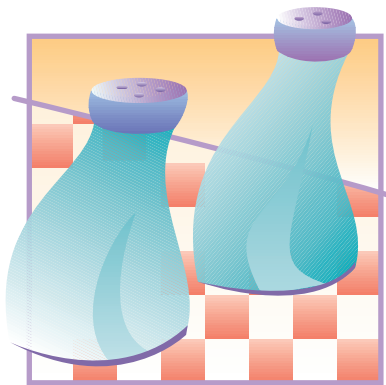
Under the *Tip Rate Determination/Education Program (TRD/EP)*, you may enter into either the TRDA or TRAC arrangement. The IRS will help you understand and meet the requirements for participation. The next pages show you how these two arrangements differ.

What's in it for me?

- A business tax credit for social security and Medicare taxes that you pay on certain employee tips
- Compliance with the law

How does the program benefit my employees?

- Greater social security and Medicare benefits
- Increased income may improve their financing approval when applying for mortgage, car, and other loans
- Increased unemployment benefits
- Increased retirement plan contributions (if applicable)
- Increased worker's compensation



TRDA vs. TRAC (how they differ)

TRDA

TRDA requires the IRS to work with the establishment to arrive at a tip rate for the various restaurant occupations.

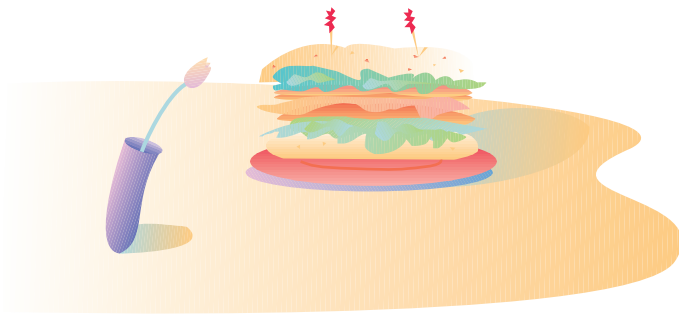
TRDA requires the employee to enter into a *Tipped Employee Participation Agreement (TEPA)* with the employer.

TRAC

TRAC does not require that a tip rate be established but it does require the employer to:

- establish a procedure where a directly-tipped employee is provided (no less than monthly) a written statement of charged tips attributed to the employee.
- implement a procedure for the employees to verify or correct any statement of attributed tips.
- adopt a method where an indirectly-tipped employee reports his or her tips (no less than monthly). This could include a statement prepared by the employer and verified or corrected by the employee.
- establish a procedure where a written statement is prepared and processed (no less than monthly) reflecting all cash tips attributable to sales of the directly-tipped employee.

TRAC does not require an agreement between the employee and the employer.



TRDA

TRAC

TRDA requires the employer to get 75% of the employees to sign *TEPAs* and report at or above the determined rate.

TRAC affects all (100%) employees.

TRDA provides that if employees fail to report at or above the determined rate, the employer will provide the names of those employees, their social security numbers, job classification, sales, hours worked, and amount of tips reported.

TRAC provides that if the employees of an establishment collectively underreport their tip income, tip examinations may occur but only for those employees that underreport.

TRDA has no specific education requirement.

TRAC includes a commitment by the employer to educate and reeducate quarterly all directly and indirectly-tipped employees and new hires of their statutory requirement to report all tips to their employer.

TRDA participation assures the employer that prior periods will not be examined as long as participants comply with the requirements under the agreement.

TRAC includes the same rule.



How To Get Your Program Underway

How To Apply

To enter into one of the arrangements, submit an application letter to your area IRS Chief, Examination/Compliance Division, Attn: Tip Coordinator. The Tip Coordinator can provide a letter format as well as extensive information on the two separate arrangements. Check your telephone directory for the IRS office in your area. They can provide the mailing address of the Tip Coordinator.

Who Should Apply

All employers with establishments where tipping is customary should review their operations. Then, if it is determined that there is or has been an underreporting of tips, the employer may apply for one of two arrangements under the *TRD/EP – TRDA, TRAC*.

Note: Employers currently under a TRDA, and wishing to switch to a TRAC, must first terminate their TRDA.

When to Apply

An employer may apply for either one of the two arrangements at any time. The effective date of the arrangement is determined by receipt and handling of the employer's application.

TRDA is effective as of the date the IRS District Director signs the arrangement.

TRAC is generally effective as of the first day of the quarter following the date the District Director signs the agreement.

For More Information

The following is a list of IRS publications and forms relating to tip income reporting that can be downloaded from the IRS Web site at www.irs.ustreas.gov and can be ordered through the IRS by dialing 1-800-829-3676. You can also get IRS forms with instructions faxed back to you when you dial (703) 368-9694 from a fax machine and follow the voice prompts.

Pub 505 – *Tax Withholding and Estimated Tax*

Pub 531 – *Reporting Tip Income*

Pub 1244 – *Employee's Daily Record of Tips and Report to Employer*. This publication includes **Form 4070**, *Employee's Report of Tips to Employer*, and **Form 4070A**, *Employee's Daily Record of Tips*.

Form 941 – *Employer's Quarterly Federal Tax Return*

Form 1040ES – *Estimated Tax for Individuals*

Form 4137 – *Social Security and Medicare Tax on Unreported Tip Income*

Form 8027 – *Employer's Annual Information of Tip Income and Allocated Tips*

Form 8846 – *Credit for Employer Social Security and Medicare Taxes Paid on Certain Employee Tips*

Form W-2 – *Wage and Tax Statement*; and separate *Instructions for Forms W-2 and W-3*





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