Tips on Tips

A Guide to Tip Income Reporting
for Employers in Businesses
Where Tip Income is Customary

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If you are an employer of an employee who receives tip income, this guide is for you.

The Internal Revenue Service (IRS) began its Tip Rate Determination/Education Program (TRD/EP) in October 1993 for businesses where tip income is customary. 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), the employer may enter into a TRDA or a TRAC arrangement, depending on the specific business. The IRS will assist applicants in understanding and meeting the requirements for participation. The next pages show how these two arrangements differ.

How does the program benefit my employees?

There are a number of reasons why an employee should report all of his/her tip income:

- Increased income may improve financial approval when applying for mortgage, car, and other loans
- Increased social security and Medicare benefits (the more you pay, the greater the benefits)
- Increased unemployment compensation benefits
- Increased employee pension, annuity, or 401(k) participation (if applicable)
- Increased workers' compensation benefits, should your employees get hurt on the job
How To Get Your Program Underway

How To Apply
To enter into one of the arrangements, you may call 1-800-829-4955 for the IRS Stakeholder Liaison Field office in your area. A Stakeholder Liaison can assist you with more information about the Tip Program. You may also obtain information by sending an e-mail to Tip.Program@irs.gov.

Who Should Apply
Currently, the IRS is offering participation in TRD/EP to employers in the food and beverage, hairstyling, and gaming (casino) industries. There are now new agreements to accommodate every tipping industry.

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 the two arrangements (depending on their specific business) under the TRD/EP - TRDA, TRAC or TRDA.

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 one of the two arrangements, depending on his/her specific business, 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 Employment Tax Territory Manager signs the arrangement.

TRAC is generally effective as of the first day of the quarter following the date the Stakeholder Liaison Area Manager signs the agreement.
## TRDA vs. TRAC

### (how they differ)

<table>
<thead>
<tr>
<th>TRDA</th>
<th>TRAC</th>
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<tbody>
<tr>
<td>TRDA requires the IRS to work with the establishment to arrive at a tip rate for the establishment’s various occupations.</td>
<td>TRAC does not require that a tip rate be established but it does require the employer to:</td>
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<td>■ establish a procedure where a directly-tipped employee is provided (no less than monthly) a written statement of charged tips attributed to the employee.</td>
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<td>■ implement a procedure for the employees to verify or correct any statement of attributed tips.</td>
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<td>■ 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 employer.</td>
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<td></td>
<td>■ 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.</td>
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<td>TRDA requires the employee to enter into a Tipped Employee Participation Agreement (TEPA) with the employer.</td>
<td>TRAC does not require an agreement between the employee and the employer.</td>
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<tr>
<td>TRDA</td>
<td>TRAC</td>
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<tr>
<td>TRDA requires the employer to get 75%</td>
<td>TRAC affects all (100%) employees.</td>
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<td>of the employees to sign TEPAs and</td>
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<td>report at or above the determined rate.</td>
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<td></td>
<td>TRAC provides that if the employees</td>
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<td>of an establishment collectively</td>
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<td></td>
<td>underreport their tip income, tip</td>
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<td>examinations may occur but only for</td>
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<td>those employees that underreport.</td>
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<tr>
<td>TRDA provides that if employees fail to</td>
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<tr>
<td>report at or above the determined rate,</td>
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<tr>
<td>the employer will provide the names</td>
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<td>of those employees, their social security</td>
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<td>numbers, job classification, sales, hours</td>
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<td>worked, and amount of tips reported.</td>
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<td>TRDA has no specific education</td>
<td>TRAC includes a commitment by the</td>
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<td>requirement.</td>
<td>employer to educate and reeducate</td>
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<td>quarterly all directly and indirectly-</td>
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<td>tipped employees and new hires of their</td>
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<td>statutory requirement to report all tips</td>
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<td>to their employer.</td>
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<td>TRDA participation assures the employer</td>
<td>TRAC includes the same rule.</td>
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<td>that prior periods will not be examined</td>
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<td>as long as participants comply with the</td>
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<td>requirements under the agreement.</td>
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Example of a TRAC Statement

Use the following “example” to help you develop your statement for your specific business, and provide a copy to your employees. (The following example is designed specifically for employees in the food and beverage industry.) A TRAC statement is given to an employee showing tips attributed to him/her. This example not only fulfills the statement required for charged tips but also for cash tip reporting and for indirectly-tipped employee reporting.
Employer Portion

Employee Name: Mark Doe
Employee Address: 123 Main Street
City, State, Zip: Any Town, USA 12345
Employee SSN: 000-00-0000
Job Category: Food Server
Establishment Name: ABC Bar & Grill
Employer EIN: 00-000000
Report Period: 01/01/00-01/31/00

Gross Sales $6,000.
Charged Sales w/Tips $2,000.
Charged Tips $280.
Charged Tip Rate 14%
Sales Subject to Cash Tips $4,000.

Employee Portion

Cash Tips $520.
Cash Tip Rate 13%

Tips Shared w/Others
Name: Job Category: Amount:
Johnny Noname Busser $120.
Total (120.)

Tips Received from Others
Name: Job Category: Amount:
Susie Cue Cocktail $100.
Total 100.

Net tips kept and reportable: $780

Employee Signature: Mark Doe Date: 2/5/00

Employer fills out top portion.

Gross Sales: only include food & drink amount. Do not include tax, tip, or non-food/drink items.
Charged Sales: include charged sales that show a tip on food & drink amounts only. Do not include tax, tip, or non-food/drink items.
(A charged sale with no tip is included as a cash sale.)

Employee fills out bottom portion.

An indirectly-tipped employee would only receive (from the employer) the “title” portion of statement filled out, unless employer captured “tips shared w/ others” information from the directly-tipped employee’s TRAC Statement and showed it as “tips received from others.” Employee signs statement and gives a copy to employer, retaining a copy for his/her records. This statement would satisfy employer's requirement under the TRAC arrangement and the employee's requirement under the law.
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 1-800-829-5676. (TTY/TDD equipment access, dial 1-800-829-4059).

**Pub 505** – Tax Withholding and Estimated Tax

**Pub 551** – 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 4157** – Social Security and Medicare Tax on Unreported Tip Income

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

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