

FOCUS ON

Tips & Gratuities in the Leisure & Hospitality sector

Income from tips often forms a large part of the income of restaurant and bar staff, however it is the employer who runs the risk of settling unpaid liabilities and penalties if tax (and national insurance contributions) are not properly accounted for.

Below is a summary of the main points that employers in the sector need to be aware of.

Income Tax

All tips received in whatever form are taxable income subject to income tax. Tips are only tax-free if no one tells HMRC about them but that's tax evasion and illegal.

PAYE on tips

PAYE is accountable on all tips except in one situation. That is where a customer pays a tip to an employee directly, or

leaves it on the table, and the employee collects it, with no involvement of the employer.

The tax will usually be collected by an adjustment to the employee's PAYE code.

Tips are often pooled and distributed by the employer or a designated member of staff, known as the troncmaster. If distributed by the employer or the employer is involved in the allocation of the tips, the employer is responsible for operating PAYE.

If distributed by the troncmaster he or she is responsible for deducting PAYE (but not NIC) and for paying it to HMRC. If an arrangement is a tronc then a business is obliged to disclose it to HMRC. If it doesn't, then the business will be held responsible by HMRC for the tax on those tips plus interest and penalties.

The employer must also notify the appointment (or replacement) of the troncmaster to HMRC. A tronc is defined as an organised arrangement for tips to be shared among employees by a person who is not the principal employer.

Sometimes employees agree informally amongst themselves to share tips and/or to give a proportion to kitchen staff. In these situations the arrangements are not usually organised and as such may not count as tronc in which case no-one has to operate PAYE if the employer is not involved at all. In these cases it is the employee's responsibility to notify HMRC of the tips received.

National Insurance (NIC)

NIC's won't be due only in the following circumstances:

- Where the tips are not paid (directly or indirectly) by the employer to the employee and they do not represent money previously received by the employer from the customer; or
- Where the tips are not allocated among the employees, directly or indirectly, by the employer.

Where NIC is payable, it is the responsibility of the employer, not the troncmaster, to account for it to HMRC.



Where the employer decides to distribute tips through their payroll alongside other remuneration the income would form part of normal income and would therefore be subject to deduction of NIC as well as PAYE.

To avoid NIC deductions the troncmaster must be independent from the business ownership and free from influence on how tips must be distributed. If they can find someone who is not management who is willing to be the troncmaster, restaurants, bars and hotels often help to set up a tronc system to avoid NIC deductions on the tips.

National Living Wage

Employees have a statutory right to the NMW, irrespective of any agreement made between the employee and the employer. For NMW purposes, employers are not permitted to take account of tips, service charges and cover charges paid by customers.

VAT on tips and service charges

Tips are not subject to VAT. Certain service charges are also outside the scope of VAT. The position depends on whether the customer has a genuine option over whether to pay the charge. This applies even where the service charge appears on the bill.

The important factor is the wording on the menu, which creates the contract between the customer and the restaurant. If it is clear that a service charge will be added, VAT is due.

But where the service charge is described as optional, no VAT is due as the customer has a genuine option as to whether or not to pay the service charge. This is the case even if it is added to the bill without asking the customer.

The distribution of service charges to staff has no effect on the VAT position. Where VAT is due, it should be deducted before payments are made to staff.

This article is only intended to provide an overview of a

complicated and high risk area and it is essential to consult with one of our tax experts if you have any concerns in relation to this subject.

Contact us

For further information, please contact a member of our Leisure & Hospitality team:



Chris Sutton
Partner

E: chris.sutton@mhllp.co.uk
T: 020 7429 4103



Huw Nicholls
Accounts & Audit Manager

E: huw.nicholls@mhllp.co.uk
T: 020 7429 4100



Chris Denning
Corporate and
International Tax Partner

E: chris.denning@mhllp.co.uk
T: 01189 503 895



David McDonnell
VAT Director

E: david.mcdonnell@mhllp.co.uk
T: 020 7429 4100



Visit our website:
www.macintyrehudson.co.uk

MHA MacIntyre Hudson is the trading name of MacIntyre Hudson LLP, a limited liability partnership, registered in England with registered number OC312313. A list of partners' names is open for inspection at its registered office, 201 Silbury Boulevard, Milton Keynes MK9 1LZ. Registered to carry on audit work in the United Kingdom and regulated for a range of investment business activities by the Institute of Chartered Accountants in England and Wales. An independent member of MHA, a national association of UK accountancy firms. The term 'partner' or 'partners' indicates that the person (or persons) in question is (or are) a member(s) of MacIntyre Hudson LLP or an employee or consultant of its affiliated businesses with equivalent standing and qualifications. Partners and directors acting as administrators or administrative receivers contract as agents and without personal liability. Further information and links to the respective regulators and appointed individuals' qualifications can be found via our website www.macintyrehudson.co.uk/information.html

MHA MacIntyre Hudson is an independent member of Baker Tilly International. Baker Tilly International Limited is an English company. Baker Tilly International provides no professional services to clients. Each member firm is a separate and independent legal entity and each describes itself as such. MHA MacIntyre Hudson is not Baker Tilly International's agent and does not have the authority to bind Baker Tilly International or act on Baker Tilly International's behalf. None of Baker Tilly International, MHA MacIntyre Hudson, nor any of the other member firms of Baker Tilly International has any liability for each other's acts or omissions. Arrandco Investments Limited is the registered owner of the UK trade mark for Baker Tilly and its associated logo.