

Pointers for Paying Out Credit Card Tips

Make sure your chosen method benefits you

Many restaurants have a very high percentage of credit card sales, and along with those tickets come tips on credit. This means the majority of the tips paid to servers are probably paid out by the restaurant owner in cash on the day the server earned the tip, while the restaurant owner waits for the cash. And as many of you can attest to, this practice can cause multiple headaches for the restaurant owners.

First and foremost, the restaurant owner's cash flow is immediately affected because they are paying cash today but waiting to receive the cash from the credit card companies, sometimes up to five days. Not to mention, if there is a chargeback, the server has still received their tip but the money never made it to the bank of the restaurant owner. I'm not advocating taking the tips back from the servers if there is a chargeback, but that is simply another place where money can sneak out of your pocket without you realizing it.

Secondly, if the restaurant is in a Tip-Credit State, which means that the restaurant pays less than minimum wage to its servers, then when it comes time for the tips to be taxed on payroll, there could be a shortfall. This is easily recognized if there are servers that receive net-zero paychecks. What has happened is their gross wages were

not enough to cover the federal and state withholding as well as the FICA and Medicare they were supposed to pay on their reported tips.

Several things could happen to take care of this shortfall and bring the check into balance. I say bring it into balance because you have to remember that accounting is all about balance. Whatever happens on one side of the journal entry has to happen somewhere else. Payroll companies could pull the shortfall out of the restaurant owner's bank account and pay the taxes anyway. They could also reduce the amount of federal and state withholding for the server to make sure there is enough payroll to cover the FICA and Medicare taxes. The FICA and Medicare taxes are not optional and do not get paid to the government at the end of the year unless you are a 1099 employee. This is the portion of the taxes that the restaurant owner also matches.

If the payroll company does decrease the amount of federal and state taxes withheld to cover FICA and Medicare, then the server will make up those unpaid taxes when they file their tax returns at the end of the year. There is no problem to the restaurant owner in this event.

The final way that the shortfall can be covered is by decreasing the amount of credit card tips that are reported for payroll. This can cause a major problem for restaurant owners because of the 8027 Tip Report required by the IRS. If you file that report and your tips reported have not been taxed, then the IRS will go back and assess penalties and fines for the entire year. They will also require amended payroll tax returns and W-2s for the servers. The IRS could go as far as to penalize the servers for underreporting their tips.

So the next question is how can you check to see if you have an



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issue? On your payroll reports that you receive for every payroll, there should be a page that shows both the employee and the employer side of the taxes taken out. The FICA/Medicare portion should be within pennies of matching exactly for the employee and the employer. If it doesn't match, you have been paying the shortfall.

Next thing to check is the total of the tips being taxed. Check that against what you reported to the payroll company. If that doesn't match, you need to have a discussion with your payroll company. I would check these places on the payroll reports every time you have a net-zero payroll check. Unfortunately, the responsibility is on the restaurant owner. If you are still uncertain as to how your payroll company is handling the shortfall, call them and ask.

Another idea for handling the shortfall is to just pay the credit card tips on the servers' payroll checks instead of paying it out every day. This simplifies matters immensely, taking care of the cash flow issue and the shortfall issue all at the same time. It may be a shock to the servers at first, but with a little advance notice on the restaurant owner's part, this could be a win-win for everyone. Heck, even the IRS would be happy!

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