



## not for profit | the national insurance treatment of tips/troncs

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The treatment for tips and troncs has been a difficult area in respect of National Insurance Contributions (NIC). The recent Employment Law case, *Nerva & others vs. ICR*, may help clarify the situation.

A tronc is a special pay arrangement used to distribute tips, gratuities and service charges. HM Revenue & Customs (HMRC) guidance was issued in December 2007. This guidance and the decision by the Courts has provided some clarification on how this process should now work and when a NIC liability will arise. Although this guidance may not appear to be good news it removes some of the uncertainty and provides Clubs with an opportunity to ensure their procedures are in line with the views of the Courts.

### what the Courts have said

Where a tronc is in place the following conditions must be met for a tronc to escape NIC:

- Management and control of that tronc must remain with the Troncmaster who must have complete and unfettered control over the funds
- The Employer is required to advise HMRC that a Troncmaster, or a new Troncmaster, has been appointed, unless the tronc arrangement existed before 6 April 2004
- HMRC will then issue a separate PAYE scheme for the tronc
- The records for the tronc must be separate from the employers payroll records
- Responsibility for the tronc PAYE scheme will rest with the Troncmaster

This is a clarification of the procedures and this is likely to be a reflection of how such arrangements should be structured in the future.

For NIC, the distinction still exists that the Employer should not be directly or indirectly involved in the allocation and distribution of the tips.

### the effect of the Court's opinion on a Staff Christmas Fund

Normally the Club Chairman requests contributions from the members of the Club to the Fund annually in advance of Christmas. Contributions from members are voluntary and the Fund may also include voluntary gratuities from functions. There are two principal ways Clubs operate a Staff Christmas Fund and they are as follows:

- **member as troncmaster** – Many clubs request a member to act as Troncmaster who is not a member of the Committee or involved in the management of the Club.

Therefore, this member is not representing the employer. As Troncmaster, the member decides on the allocation of the Fund to the appropriate employees.

- **staff committee** – A small number of employees are appointed by the staff to administer the allocation and distribution of the Fund.

## tips and VAT

Tips (sometimes referred to as discretionary service charges) are outside the scope of VAT when they are given at the absolute discretion of the customer, even if the amounts appear on the bill (provided it is clear that the amount is discretionary). It does not matter if the payment made by the customer is in cash, by cheque/credit/debit card, nor does it matter if the tips are actually passed to the staff. The important point is that the customer must be free to pay nothing if he/she so chooses. If a mandatory service charge is added then VAT is due on that as well as the price of the meal.

It was agreed in the early 1990s with the Contributions Agency that these types of arrangements do not attract a National Insurance liability.

In the light of the Nerva case, we recommend that you consider replacing the member, who is currently the Troncmaster of the Christmas Fund, with an employee, who is not in a management role. It would also be prudent to ensure that the allocation of the Fund is based on a points system or a formula set by a Staff Committee.

Alternatively, you can either continue with the current arrangement on the understanding that HMRC may challenge the process or seek further clarification from HMRC.

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