

TIP AUDIT NEWS

Morrison vs. IRS

and the winner is...*not* the IRS!

Good news for restaurateurs everywhere—the U.S. District Court in Alabama ruled in favor of Morrison Restaurants Inc. in their suit against the IRS requesting a refund of employer taxes assessed by the IRS.

The IRS conducted a tip audit on one of Morrison's Ruby Tuesday restaurants (in Pensacola, FL) and assessed employer FICA based on the McQuatter's Formula.

The Alabama court ruled that there is no statutory basis, or law, that allows the IRS do that because:

- ✓ the IRS did not first audit the employees to determine if, in fact, there was under-reporting of tips;
- ✓ only the employer was assessed

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the FICA tax, not the employees;

- ✓ the employee's individual Social Security accounts received no benefit from this employer assessment.

Basically, the Alabama court undermined the TRDA program the IRS had been trying to use to enforce tip reporting, putting the burden on the employer. The TRDA (Tip Rate Determination Agreement) requires employers and employees to pay FICA taxes on an agreed-upon percentage of receipts, regardless of the actual amount received in tips. (Please see the comparison table on page 2.)

The Morrison case decision doesn't provide protection against an employer assessment based upon an audit of individual employees. The IRS is still aggressively pursuing sign-ups of the more reasonable TRAC (Tip Reporting Alternative Commitment) agreements. While the IRS does not have the resources to conduct individual audits of all tipped employees, it certainly can

audit the tipped employees of a single "uncooperative" restaurant.

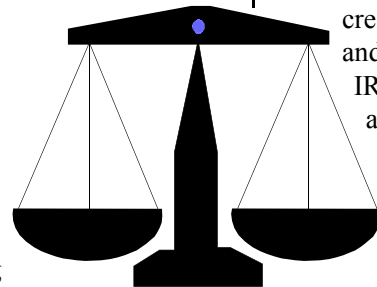
The IRS is unlikely to be deterred in its pursuit of taxes on tip income.

But, the Morrison decision *does* create a problem for the IRS, and employers should find the IRS more willing to negotiate and grant refunds of previous assessments.

That's not to say that the IRS is going to give up on employer-only audits. The Morrison case affects only the

Southern District of Alabama and the IRS will probably file an appeal with the U.S. Court of Appeals for the 11th Circuit.

But more court cases are on the



Coming soon to your neighborhood — ***PayMaster* version 7.2!**

- *PayMaster* with 6 jobs, each with regular, overtime, and miscellaneous rates.
- New tip report now includes cash tips percentage and charged tips percentage for each employee.

horizon—and everyone is watching them closely.

Continued on page 2.

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continued from page 1.

The National Restaurant Association's case on behalf of the Bubble Room (Orange City, FL) is in the Court of Federal Claims, so it will have national impact. A decision is not expected for at least another year. And it's likely that whoever loses will appeal, which would probably take another two years to resolve.

In a case similar to Morrison's, the Riese Organization (who coincidentally is using the same attorney that Morrison's used—Tracy Power of Power & Power in Arlington, VA) has filed a complaint in U.S. District Court for the Southern District of New York.

The Riese Organization had eight Manhattan restaurants audited, and was assessed employer-only FICA based on the McQuatter's Formula.

And, as in the Morrison audit, no employees were audited or assessed, and the employees' Social Security accounts received no benefit.

What does this mean for you?

If you previously paid an IRS assessment for employer-only FICA taxes on IRS-estimated unreported tip income, consider immediately filing for a refund of taxes paid and/or an abatement of taxes assessed.

If you signed a TRAC, what should you do? And how can Computer Aid and PayMaster help you?

1. Order a copy of the IRS video titled "*Reporting Tip Income: on TRAC*" to show your new employees and current employees on a quarterly basis.

See page 8 of this issue of **THE BLUE PAGES** for information about this video (VHS format) and how to obtain a copy from

Computer Aid Corporation.

2. Use *PayMaster's* feature that allows payment of charged tips in net pay. This eliminates the possibility of under-reporting of charged tips (for which there is an audit trail).
3. Use *PayMaster* to track the information needed for your annual Form 8027. And review it on a regular basis.
4. Notify tipped employees that their *PayMaster* check stub shows receipts and tips.
5. Use *PayMaster's* tip report as a sign-off sheet when employees pick up their paychecks to verify that their reported tips are correct.

PayMaster 7.2 (shipping later this summer) will have a tip report showing not only cash & charged receipts and tips by employee, but also showing each employee's cash and charged tip **percentage**. (see related article on page 4)

Current law compared to TRAC & to TRDA			
ER = Employer EE = Employee	Current Law	TRAC	TRDA
Tip Reporting	EE is required to report tips in writing to employer by the 10th of the following month.	ER must establish a procedure for recording charged tips on an EE-by-EE basis. EE signs to verify receipt of tips or to indicate correct amount, taking into consideration tip-outs. ER must establish a reasonable method for reporting charged tips received by indirectly tipped EEs. ER must establish a procedure for EEs to report cash tips. Procedure may be similar to procedure for charged tips.	Participating EEs report charged tips and cash tips at a fixed percentage of total sales, even though they may receive less than the fixed rate. Tip rates are determined by the IRS based on the "McQuatter's" formula and historical data on tips for the establishment's employees.
Educational Requirements	IRS issues instructions and publications on tip reporting, but ERs are not required to distribute this information to EEs.	ER is required to educate all tipped EEs quarterly to understand that the law requires all tips be reported.	No specific educational requirements, but ERs typically must explain to EEs the TRDA system and warn EEs of the increased audit risk if 75% do not comply.

6. Use *PayMaster* to print the FICA Credit on Tips report so you can take the tax credit when you file your corporate income taxes.

Continued on page 3.

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continued from page 2.

What should you be doing even if you haven't signed a TRAC?

1. Educate your employees—the law is that they are to report 100% of their tips.
2. Make sure that indirectly tipped employees are reporting their share of the tips.
3. Ensure that you are reporting the correct amount of charged tips—which should be possible since you have an accurate (and auditable) figure for them.

4. File your annual form 8027—reporting cash and charged tips and receipts.
5. Make sure you take your tax credit on Employer FICA on Excess Tips (not required, but hey, it's to your benefit).

When you use *PayMaster* and take full advantage of its features, you know what your employees are reporting:

- ◆ cash receipts by server for each payroll,
- ◆ charged receipts by server for each payroll,
- ◆ cash tips & tip percentage by server for each payroll,

- ◆ charged tips & tip percentage by server for each payroll,
- ◆ tips received by indirectly tipped employees, and
- ◆ total receipts and total tips for the division and the percentage of tips to receipts.

Be prepared. Keep informed about the law, the IRS programs, the court case decisions, and the *PayMaster* reports that show what your employees are reporting as tips.

With knowledge, you can make decisions with confidence.



Order form for IRS "Reporting Tip Income: on TRAC" video		
Yes, I want a painless way to educate my employees about tip reporting laws. Please send me [] copy(ies) of the IRS video: "Reporting Tip Income: on TRAC". (VHS format)	Single copy price — \$25 Multiple copy price — \$20 each Price includes shipping & handling	\$
	VA residents, please add 4.5% sales tax.	\$
	COD orders, please add \$7.50 COD charge.	\$
All orders must be prepaid, COD, or charged to a credit card. We accept VISA, MasterCard, American Express, and Discover.	TOTAL	\$
Indicate payment type: [] check enclosed [] COD [] credit card		
Credit card number:	Expiration date:	Authorized signature:
Ship to: Name		
Company		
Street Address		
City/State/Zip		
Area code/phone	Fax	

Send form with payment to:	Computer Aid Corporation P.O. Box 1074 Vienna, VA 22183	Credit card and COD orders can be faxed to 703-281-3461
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***PayMaster's* new tip report**

PayMaster version 7.2, available later this summer, incorporates more information into the tip report, illustrated below.

Now you'll be able to see not only the individual server cash and charged receipts and tips, but also the percentage for cash tips and the percentage for charged tips for each server.

Many *PayMaster* users are eagerly awaiting this feature. Some, who have already signed a TRAC agreement, are using this report to fulfill one of their TRAC requirements.

Taken from a copy of a TRAC agreement example, the requirement reads that:

“...the Establishment must establish a procedure under which a written statement is prepared and processed on a regular basis (no less frequently than monthly) reflecting all charged tips for sales attributable to each directly tipped Employee. The Establishment must implement reasonable procedures under which each directly tipped Employee is given the opportunity to verify or correct any statement of proposed attribution of charged tips, in order to reflect tip outs, tip sharing, tip pooling, and other adjustments.”

“For example, the Establishment would satisfy this paragraph if it provided a written statement that contained the following information: Employee's charged sales, Employee's total charged tips, and the ratio of a percentage, of charged tips to charged sales.”

“The Establishment must also adopt a reasonable method for reporting of charged tips received by indirectly tipped Employees...the Establishment could furnish the indirectly tipped Employee a written statement, which that Employee would verify or correct in a manner similar to the procedure for directly tipped Employees.”



Tax law changes

Federal

- **Minimum wage increase?** No word yet as we go to press.

If it happens, there are changes you must make in *PayMaster* in the Company, Division, and Employee files.

If you're not sure what to do, ask us to fax our Minimum Wage Increase Checklist to you.

- **Form 4070—Employee's Report of Tips to Employer**—is being revised.

Previous versions allowed the reporting of only *total* tips. The new version will allow separate reporting of cash tips, charged tips received, and tips paid out to other employees.

Payment System).

Before you can deposit electronically, you must enroll in EFTPS—and the enrollment process takes at least 12 weeks to complete.

Failure to complete the enrollment process in time will be expensive. There's a **10% avoidance penalty** for using the paper form 8109 if electronic deposit is mandated.

If you know you are mandated and haven't received a notice from the IRS by September, contact the appropriate EFTPS financial agent.

For employers in the Mid-Atlantic, South, Southwest, and southern California, it's Nations Bank (1-800-555-4477).

For employers in the Northwest, Midwest, Northeast, and northern California, it's First Chicago Bank (1-800-945-8400).

The Summer 1996 issue of the SSA/IRS **Reporter** that comes with your 941 form has an article on the new EFTPS, with a map illustrating which of the two banks each state calls.

MN Required effective 7/1/96.

State minimum wage

DE \$4.65/hr; \$2.32/hr tipped employees, effective 4/15/96.

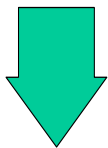
\$5.00/hr; \$2.50/hr tipped employees, effective 1/1/97.

VT \$5.00/hr; \$2.65/hr tipped employees, effective 1/1/97.

\$5.15/hr; \$2.68/hr tipped employees, effective 1/1/98.

State new hire reporting

New IRS Requirement— Failure to comply could mean large penalties.



- **Electronic filing of federal tax deposits**—Form 8109 (Federal Tax Deposit Form) is on its way out for many employers.

Effective 1/1/97, employers with employment tax liabilities of at least \$50,000 during 1995 are **required** to file federal tax deposits electronically using EFTPS (Electronic Federal Tax

☐ State withholding

New withholding tables for:

CT effective 7/1/96.

KY new local tax for Wolfe County, effective 2/1/96.

NY effective 4/1/96.

OH local tax changes for various cities, villages, and school districts, effective 7/1/96.

UT effective 7/1/96.



Q&A

Q. I noticed a mistake I had made on an employee's check (wrong pay rate), after I had already updated the files and printed the checks. I thought *PayMaster* would let me “make corrections?”, but when I went to RESUME, it doesn't ask this question anymore? How can I make this correction?

A. *PayMaster* didn't ask if you want to make corrections because, in order to print the checks, you first had to update the payroll files (month-to-date, quarter-to-date, and year-to-date).

Any corrections you make at this point should be done using *PayMaster* to void the check and issue a select check.

You do have the option of manually voiding the check, handwriting another, and going

into the employee's MTD, QTD, and YTD date files to manually change the data, but that's a lot more work, and much more prone to error. And, it will mess up your bank reconciliation if you use *PayMaster* for reconciling. Using *PayMaster* to void and re-issue is much easier.

Q. When I use *PayMaster*'s UTILITY menu to back up my payroll data, it doesn't always work. Some times it's fine and the filenames appear on the screen as each is “zipped” and copied to the floppy. Other times, something flashes quickly on the screen and then disappears, leaving me in the menu. What's happening?

A. Occasionally, you'll not have enough memory for PKZIP (the file utility used by *PayMaster* to back up your files to a floppy

disk) to zip and copy the files.

It's best, before backing up from *PayMaster*'s UTILITY menu, to exit from *PayMaster* first. Go back in and then choose BACKUP from the UTILITY menu. It should work fine. (We're adding a note to the next version of *PayMaster* to remind you to do this whenever you use *PayMaster*'s backup.)

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Throughout THE BLUE PAGES, there are references to payroll tax laws and requirements in effect as of the dates specified. These references to the laws and the explanations provided are designed to familiarize the employer with said laws, but are not meant to serve either as a legal or accounting opinion, or as any indication that reference to the Internal Revenue Code or Regulations issued thereunder and appropriate administrative or court rulings interpreting same is unnecessary. All persons using this newsletter should look to and rely upon their respective legal counsel and accountants with respect to these laws and requirements.

st payroll and wanted to restore my old files and just start over, but I was afraid I would mess up things even more. So I ended up voiding a lot of checks and reissuing them instead. Next time, to restore my files to start fresh, what should I do so I can feel confident about restoring them safely?

A. **First**, print a payroll summary of the current data.

Second, do a backup of the current files, just in case. And, do this twice—once on a floppy disk and once on the hard drive:

1. For the floppy backup: Exit *PayMaster* and go back in. From the UTILITY menu, select BACKUP. PKZIP will zip and copy your files to the indicated floppy drive.
2. For the hard disk backup: In *PayMaster*, go to INIT, COMPANY to see where your data is stored. (For example: C:\PRV7\FLORA).

Exit *PayMaster* and change directories so you're in the data directory.

(Example: *cd c:\prv7\flora*)

Copy the dat files as bak files, by entering:

copy py.dat py*.bak*

Third, restore your backup:

From the *PayMaster* menu, choose UTILITY, RESTORE. *PayMaster* will take the data from the floppy and write over the data on the hard drive.

Important. PKUNZIP, which is used by *PayMaster's* RESTORE, asks if you want to overwrite the files. Respond **A** for **All**.

Fourth, print a payroll summary. Before using this data, you want

to double check that it's the data you are expecting.

Q. Have they passed the Minimum Wage bill yet? What do I need to do in *PayMaster* if there's an increase in the minimum wage?

A. As we go to press, no final action has yet been taken. See the note on page 5 (Tax law changes).

Q. Does Computer Aid take credit cards?

A. Yes, we now accept Visa, MasterCard, American Express, and Discover.



User spotlight on Ground Round & Howard Johnson's

“With PayMaster's input sheet and batch screens, it takes a lot less time to enter each employee's data and to process payroll.”

John Keeley, Vice President,
Connecticut Foods, Inc.

John Keeley started his professional career in public accounting. One of the clients for whom he did work was Connecticut Foods, based in Milford, CT. He joined their staff 32 years ago as an accountant and he is now Vice President.

Connecticut Foods has a Ground Round and three Howard Johnson's restaurants located in Fairfield, Milford, New Haven, and Branford, CT.

They also provide accounting and book-keeping services for over 20 restaurants in Florida, Pennsylvania, and New England, and process payroll for a restaurant in Massachusetts and Rhode Island.

John says, “In 1987, I was using an IBM System 23 with custom payroll and accounting software. The system had three terminals and a 30MB hard drive and, with the software, cost about \$30,000. It was working fine, but the company that had written the custom software was out of business, so we could no longer get updates of the payroll software. And, the hardware maintenance was costing us \$4,000 a year.”

“When I started to look for new software, I got the names of several vendors of restaurant payroll software from the National Restaurant Association. I narrowed the choices down to two: a company in Virginia and another in California.

It turned out that both companies sold the same software (*PayMaster*) developed by the company in Virginia—Computer Aid Corporation.”

“I selected *PayMaster* because it was exactly what I was looking for. It has multiple jobs and pay rates, and lets you use meal deductions. It handles tips so well and works a lot better than my old system. With *PayMaster's* input sheet and batch screens, it takes a lot less time to enter each employee's data and to

John Keeley of Connecticut Foods at Computer Aid's booth at the New York show.

process payroll.”

“Since some of our employees work more than three jobs, we're looking forward to the new release of *PayMaster* that has six jobs.”

“After using *PayMaster* for a couple of years, I added CharterHouse accounts payable and general ledger, because *PayMaster* interfaces to it. It's excellent and very user-friendly compared to other accounting

programs. It's got a variety of reports.”

“I especially like the 12-column spreadsheet that lets me see a year's activity at a time. Some of my companies use budgets; others use current and prior year activity. It is very flexible and easy to operate.”

“We have three data entry personnel. With their help, Ellen Carter, one of the owners of Connecticut Foods and the Director of Human Resources, is able to do all of the payrolls for the six restaurants in one day.”

Ellen says, “When I first started using *PayMaster* five years ago, I was totally computer illiterate. It was easy to learn how to use the program—it's very user-friendly. And, I feel very comfortable that it's accurate.”

John says, “We've used *PayMaster's* 8027 report from the beginning and have always reported all charged tips. Since we have coffee shops, many of our customers tip in cash.”

“When employees are hired, the manager talks to them and explains that all tips should be reported. We also have signs in the employee area reminding staff about tip reporting. Fortunately, the IRS has never knocked on our door. If they do, I think they'll find everything in order.”



Pay Master Tip

*Back up your payroll data on **alternating** diskettes, keeping at least three versions.*

Then, at any time, you will always have on floppy disks the last payroll, the second last payroll, and the third last payroll.

The next time you back up the data, take the oldest disk and use it over again.

New video release from the IRS

Yes, the IRS has released a video—*“Reporting Tip Income: on TRAC.”* Doesn't have much of a plot, and it's not on the “Best Seller” list, but it is very popular and hard to get.

Q. What is the video about?

A. It's about reporting tips and the tax law—How? Who? What? Where? And Why?

Q. What do you do with this video (assuming you've got better things to watch on your VCR)?

A. You show it to your directly and indirectly tipped employees, when they are hired, and again on a quarterly basis. This can be done voluntarily or as part of a TRAC agreement you may sign with the IRS.

Q. Can I get a copy from the IRS?

A. It's difficult and maybe impossible. The IRS made a limited number of 3/4 inch masters, which they have been lending only to large corporations, giving them permission to reproduce it. They have none to lend at the present time, until some of the masters are returned. And, there's a waiting list.

Q. Is there an easy way to get one of these tapes?

A. We've made it easy for you. We were one of the first to put in a request and actually got a copy, which we have duplicated for resale, with the IRS's approval.

You can order a copy from us for a nominal fee and you'll have it within days. Multiple copies are available at a discount.

Be a step ahead of the IRS.

Voluntarily do some of the things they're requiring of TRAC signers—before they get to you.

So, pull up a chair. Pass the popcorn, and enjoy the show!

Please see the order form for the IRS video on page 3.

“Tips on Tips” available from the IRS — if you act quickly

Pub 1875 “Tips on Tips” for employees & Pub 1872 “Tips on Tips” for employers were printed in limited quantities. Because of budget restrictions, the IRS will not reprint them. For copies, call their forms line (1-800-829-3676) or the IRS Education Dept at 1-800-829-1040.



IRS loses to restaurant industry

Story on page one.