



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D C. 20224

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MEMORANDUM FOR ALL INDIAN TRIBAL GOVERNMENTS EMPLOYEES

FROM: Angela Gartland /s/ *Angela Gartland*
Acting Director, Government Entities

SUBJECT: Procedures to Conduct Tip Agreement Compliance Reviews

Purpose:

This memo's purpose is to provide procedures on conducting tip agreement compliance reviews as described in IRM 4.88.1. It includes procedures for each possible outcome and examples of when it may be warranted to revoke a tip agreement.

Background:

As part of Indian Tribal Governments (ITG) Tip Program responsibilities, we annually monitor tip agreements. We create a case file when we identify potential non-compliance typically containing, Forms 8027, Employer's Annual Information Return of Tip and Allocated Tips, (if available) for the current and two prior years; Annual and Quarterly Employee Reports; and Employee Time and Attendance Reports.

Procedural Change:

The compliance review is assigned to an ITG specialist to conduct the review, which is made up of the following phases:

- 1) Precontact Analysis
- 2) Taxpayer Contact
- 3) Compliance Review
- 4) Case Summary and Disposition

Examiner's Responsibilities:

- 1) Precontact Analysis: Before you contact the taxpayer, conduct and document the precontact analysis, which includes some or all of the following:

- Review the tip agreement, including any addenda, prior extensions and economic rate reductions to gain familiarity with the existing agreement.
- Research the internet to determine if the taxpayer has any change in business ownership, locations, branding and/or types of business activities or workers.
- Research IDRS to determine the taxpayer's filing and payment compliance and to secure reported wages and tips and gross receipts for the current and two prior years.
- Analyze the above information to determine if the current and two prior years of reported tips are reasonable and consistent.
- See the following examples of situations where the analysis may indicate non-compliance with the tip agreement:
 - Material change in sales, but minimal change in reported tips
 - Non-tippable sales on Form 8027 inconsistent with industry standards
 - Minimal change in sales, but material change in charged tips or number of employees on Forms 8027
 - Tip rate calculated using Form 8027 data is inconsistent with tip rates on current tip agreement
 - Discrepancies between Total Tips reported on Forms 8027 and Total Medicare and Social Security Tip Wages reported on Forms 941
 - Questionable allocation of tips on Forms 8027

2) Taxpayer Contact: After completing the precontact analysis, send a letter to the taxpayer to notify them of the compliance review. Include an Information Document Request (IDR) to request only the necessary information that applies to each establishment. Request this information to determine if the taxpayer's procedures and internal controls to report both direct and indirect tips comply with the tip reporting requirements of the tip agreement.

Examples of commonly requested records and documents include:

- Confirmation of the legal corporate name, d/b/a, physical address, tribally designated individuals with signature authority (and title)
- Name and EIN of entity filing Forms 941 and W-2
- Documentation of the program and materials used to educate new and existing employees about their tip reporting requirements
- Written procedures requiring directly tipped and indirectly tipped employees to report tips
- Documentation of the process used to ensure all reported tips are included on Forms 941 and W-2

- List all establishments covered under the tip agreement
- List of all tipped positions, tip rates, and number of tipped employees in each position
- Policy and procedures for handling service charges and auto gratuities
- List of systems used to track tips and prepare annual reports: point of sale, payroll, timekeeping, etc.

You may call the taxpayer 15 days after you mail the IDR to schedule an appointment for onsite visits, interviews, walkthrough of the tip reporting process, and to review the IDR response.

3) Compliance Review: Refer to IRS training course number 28136-002, Combined Tip/Gaming Training, for guidance in conducting the compliance review. The course material includes:

- Reviewing Internal Controls
- Calculating Participation Level
- Evaluating payroll procedures
- Determining if tip agreement requires modification
- Determining if the employer is complying with the tip agreement commitments
- Analyzing Form 8027 data, samples to illustrate the process, and issues which you may encounter

Summarize your findings and document interviews, tours taken (if any), three-year comparative analysis, overall tip reporting compliance analysis, etc.

Document the case file workpapers with your review steps and include relevant supporting documents and records.

Consider revocation of the tip agreement if any of the following fact patterns are present:

- The taxpayer has failed or refuses to establish and maintain an Employer-Computed Tip Reporting Process per the GITCA Tip Agreement, Section V, paragraph J.
- Analysis of GITCA or TRDA year-end reports shows a substantial underreporting of tips for two consecutive years and or the taxpayer has failed or refuses to implement the procedures to timely and accurately report the required data.
- A large food and beverage taxpayer hasn't filed Forms 8027 for two or more years after the ITG Tip analyst has sent them annual reminders via certified mail/return receipt.
- Comparative analysis of three years of tax return data shows stable gross sales and wages, but tips reported on Form 941 and or Form 8027 decreased substantially, and a

review of external source information gathered through taxpayer contact indicates the business activity has not changed significantly.

- 4) Case Summary and Disposition: Prepare Form 14354, Summary of Compliance Review Findings and Recommendations, and forward the case file to your group manager for review and approval. Get your manager's approval of the recommended disposition **before** notifying the taxpayer of the review outcome.

The three potential outcomes for a compliance review are: no change, change and revocation.

1. Recommended "No Change" to tip agreement: Submit Form 14354 to the group manager for review and approval. After your manager approves the recommendation and documents the case file activity record, notify the taxpayer of the results by issuing Form 14354. Close the case to the group manager within 15 days. The group manager forwards it to the ITG Tip analyst within 15 days.
2. Recommended "Change" to tip agreement: Prepare Form 14354-A, Compliance Review Acceptance Statement. Submit Forms 14354 and 14354-A to your manager for review and approval. After your manager approves the recommendations and documents the case file activity record, notify the taxpayer of the results by issuing Forms 14354 and 14354-A.
 - a) If the taxpayer accepts the recommendations, signs and returns the Form 14354-A, and implements the necessary changes by the corrective action due date, close the case to the group manager within 15 days.
 - b) If the taxpayer accepts the recommendations but can't implement the necessary changes by the corrective action due date, you may grant up to an additional 90 days with your manager's approval. Group manager's approval must be documented in the case file. Revise Form 14354 with the new corrective action due date. Reissue Forms 14354 and 14354-A with the revised date and secure the taxpayer's signature. Place the case in suspense (status 15) and hold in the group until the response due date. Close the case to the group manager within 15 days of determining the taxpayer carried out the corrective actions.
 - c) If the taxpayer doesn't address the corrective actions by the response due date or accept the recommendations, revoke the tip agreement.
3. Recommended "Revocation" of tip agreement: Prepare Form 886-A, Explanation of Items, documenting deficiencies. Submit Forms 14354 and 886-A to the group manager for review and approval. After your manager approves the recommendation and documents the case file activity record in the case file, notify the taxpayer of the results by issuing Forms 14354 and 886-A. Offer the taxpayer an informal conference. If the taxpayer declines to participate or if there's no resolution from the informal conference, close the case to the group manager within 15 days. The group manager forwards it to the ITG Tip analyst within 15 days to finalize the revocation.

Effect on Other Documents:

We'll incorporate this guidance into IRM 4.88.1, Examination Issues Pertaining to ITG Cases, by July 15, 2022.

Effective Date:

This memo's effective date is July 15, 2020.

Contact:

If you have questions about this guidance, please contact Telly Meier, Program Manager Indian Tribal Governments.

Distribution:

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