



OFFICE OF
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The Honorable Michael C. Burgess
Member, U.S. House of Representatives
2000 South Stemmons Freeway, Suite 200
Lake Dallas, TX 75065

Attention:

Dear Representative Burgess:

I am responding to your inquiry dated March 13, 2019, on behalf of your constituent, . asked about the tax reporting requirements for nail salon workers who receive cash payments. Specifically, explained his concerns about possible underreporting of income by workers in this industry.

This information letter highlights certain general principles of law. It is intended for information purposes only and does not constitute a ruling. See Rev. Proc. 2019-1, Section 2.04, 2019-1 I.R.B. 1, (January 2, 2019).

Section 61(a)(1) of the Internal Revenue Code (Code) provides that gross income means all income from whatever source derived, including, but not limited to, compensation for services, including fees, commissions, fringe benefits and similar items. Section 1.61-2(a)(1) of the Income Tax Regulations provides that tips are income to the recipients.

Sections 3101 and 3111 of the Code impose Social Security and Medicare taxes under the Federal Insurance Contributions Act (FICA) on employees and employers, respectively, equal to a percentage of the wages received by an employee with respect to employment. Section 3121(a) defines wages for purposes of the FICA tax as all

remuneration for services performed by an employee for an employer, with certain exceptions. Section 3121(a)(12) provides that cash tips of \$20 or more received by an employee in any calendar month in the course of the employee's employment are wages for FICA purposes. Similar rules are provided in sections 3401(f) and 3402(k) as they apply to income tax withholding.

The Code establishes a set of specific rules that govern tip reporting. The fundamental rule is that an employee must report tips received to his or her employer. This rule is found at section 6053 of the Code and requires every employee who receives more than \$20 in tips a month to report those tips to their employer on a written statement no later than the 10th day of the month following the month in which the employee received the tips.

Section 6051(a) requires employers to provide employees with a written statement (Form W-2) each year showing, among other things, the amount of wages paid and the amount of income and employment taxes deducted and withheld. Under section 31.6051-1(a)(1)(vi) of the regulations, tips reported by the employee to the employer under section 6053(a) are reported as wages on Form W-2.

Self-employed individuals generally are responsible for filing and paying all their own taxes, which includes self-employment tax as well as income tax. Self-employment tax is a Social Security and Medicare tax primarily for individuals who work for themselves. It's similar to the Social Security and Medicare taxes withheld from the pay of most wage earners. Tips received by self-employed individuals should be reported as income on Schedule C, Profit or Loss from Business. Self-employed individuals can get more information about reporting in Publication 334, Tax Guide for Small Business on our website at www.irs.gov, click on Forms & Publications.

If the IRS determines that a worker underreported their tips, they could be subject to additional federal income tax, Social Security and Medicare taxes. Penalties and interest may also apply.

I'm enclosing a copy of Publication 531, Reporting Tip Income, which provides guidance for employees who receive tips. I'm also enclosing a copy of Publication 3144, Tips on Tips, which gives guidance to tip income reporting for employers in businesses that usually generate tip income.

Again, this letter is intended for information purposes only and does not constitute a ruling. I hope it is helpful. If you have additional questions, please contact me or at .

Sincerely,

Melissa L. Duce
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(Employee Benefits, Exempt Organizations
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