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INTERNAL REVENUE SERVICE

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NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

District Director

Taxpayer's Name:

Taxpayer's Address:

Taxpayer's Identification Number:

Years Involved:

Conference:

Legend

Taxpayer =

ISSUE:

Whether Taxpayer may claim the credit under section 45B of the Code with respect to all tips received by its employees, or is the credit limited to tips received in connection with its unrelated business activity?

FACTS:

Taxpayer is a social club exempt under section 501(c)(7) of the Code. It operates a country club with a private golf course and related amenities. As part of the country club operation, Taxpayer has a large clubhouse where food and beverages are served to members and their guests. Waitresses and busboys are paid by the hour and also receive tips. The tips are allocated to the workers and are reported on Taxpayer's employment tax returns. FICA and Medicare tax is also paid on the reported tips.

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Taxpayer allows its members to sponsor private parties. The income from these parties is reported as nonmember income on Form 990-T, Exempt Organization Business Income Tax Return. Taxpayer has filed amended Forms 990-T for fiscal years 1994 - 1996 to claim credit under section 45B of the Code for employer social security and Medicare taxes paid on employee tips. Taxpayer calculated the credit based on all tips received by its employees rather than calculating the credit only on the tips received with respect to its unrelated business activity. The excess credit was carried back to the earlier years.

LAW AND ANALYSIS:

Section 45B of the Code describes a business tax credit allowable under section 38 for the employer portion of FICA tax paid on employee tips.

Section 45B(a) defines the credit in terms of the "excess employer social security tax" paid or incurred by the taxpayer. Section 45B(b)(1) defines "excess employer social security tax" as any tax paid by an employer under section 3111 with respect to tips received by an employee during any month, to the extent those tips (A) are deemed to have been paid by the employer to an employee under section 3121(q) (without regard to whether the tips are reported under section 6053), and (B) exceed the amount by which wages (excluding tips) paid by the employer to the employee during that month are less than the total amount that would be payable (with respect to that employment) at the minimum wage rate applicable to the individual under section 6(a)(1) of the Fair Labor Standards Act of 1938 (determined without regard to section 3(m) of that Act).

Section 45B(b)(2) limits the tips that can be taken into account for purposes of section 45B to those tips "received from customers in connection with the providing, delivering, or serving of food or beverages for consumption if the tipping of employees delivering or serving food or beverages by customers is customary."

Section 45B(c) disallows any deduction for any amount taken into account in determining the credit under section 45B. Section 45B(d) allows a taxpayer to elect not to claim the credit for any taxable year.

The section 45B credit has the effect of limiting the employer's employment tax liability to the amount that would be

due if the employee received only the minimum wage, no matter how much the employee actually earned. The employee's earnings record and individual income tax liability are unaffected.

Taxpayer has paid FICA taxes on all tips earned by its employees. These tips meet the requirements of section 45B(b)(2). Section 45B does not prohibit tax-exempt organizations from claiming the credit, nor does it limit the credit the credit to FICA taxes associated with an unrelated business activity. Therefore, Taxpayer is allowed to calculate the section 45B credit on the basis of all tips received by its employees, not just the tips received in the unrelated business activity.

CONCLUSION:

The credit provided under section 45B of the Code is an allowable credit against unrelated business income tax. The tax credit is not limited to the taxes associated with the unrelated trade or business activity. The credit may be claimed with respect to all tips received by Taxpayer's employees.