**Private Letter Ruling**

|  |  |
| --- | --- |
| **Ruling Number:** | **P-1999-45** |

|  |  |
| --- | --- |
| **Tax Type:** | **Kansas Retailers' Sales Tax** |
| **Brief Description:** | **Automatic gratuities or service charges.** |
| **Keywords:** |  |
| **Approval Date:** | **03/01/1999** |

**Body:**

Office of Policy & Research  
  
March 1, 1999

XXXX  
XXXX  
XXXX

RE: Your letter dated January 6, 1999

Dear XXXX:  
  
I have been asked to answer your letter that we received last month. In it you ask if service charges that are automatically billed by a private club (the “Club”) to its members as a percentage of food and drink charges should be treated as belonging to the club or belonging to the servers for income tax purposes.  
  
Automatically imposed services charges are sometimes called mandatory gratuities, which is somewhat of a oxymoron. The Kansas Department of Revenue litigated whether such charges are subject to sales tax in *In re Tax Appeal of Newton Country Club*, 12 Kan. App. 2d 638, 753 P.2d 304 (1988). The Kansas Court of Appeals upheld the department’s position that these charges are part of the taxpayer’s gross receipts and must be included in the tax base for Kansas sales tax and liquor excise tax.  
  
Your question does not involve sales tax, which you indicate the Club is collecting on the service charges. You ask whether these charges belong to the Club or to the servers. You state:

At one time the Club distributed a portion of these automatic charges to its servers. In May of 1993 the servers voted approval of a change in their own method of compensation so that instead of a low base rate and a share of the automatic charge, they received a higher flat rate several dollars in excess of the state and federal minimum wage, but no portion of the automatic charge.

This statement indicates that the automatically imposed service charge belongs to the Club and, therefore, are proceeds of the Club rather than proceeds of the servers for purposes of income tax. This is consistent with the rationale expressed in *In re Tax Appeal of Newton Country Club*. No part of the receipts should be accounted for as tips or wages for income tax purposes since the Club does not disburse the receipts to service employees.  
  
The fact that a patron may view the service charge as being a tip would not overcome the agreement between the Club and the servers about wages and treatment of the automatic service charge. These charges are part of the Club’s income. Therefore, no part of the receipts should be treated as tips or wages for income tax purposes.  
  
Please note that this opinion is based on your description of the contract between the Club and its employees rather than on a review of the contract itself. It assumes that you have provided all the material facts required to form an accurate opinion. I hope that the discussion adequately answers your questions. If not, please call me at (785) 296-3081.

Sincerely,  
  
  
Thomas E. Hatten

Attorney/Policy & Research  
  
  
**Date Composed: 03/17/1999 Date Modified: 10/11/2001**