

ST 24-0019-GIL 04/22/2024 MANDATORY SERVICE CHARGE

Mandatory gratuity charges which are separately stated and paid directly by a retailer to its service employees are not subject to tax provided that the proceeds of the service charge are in fact turned over as tips or as a substitute for tips to the employees who participate directly in preparing, serving, hosting, or cleaning up the food or beverage function with respect to which the service charge is imposed. See 86 Ill. Admin. Code 130.120(r); 86 Ill. Admin. Code 130.2145(d). (This is a GIL.)

April 22, 2024

NAME
ADDRESS

Dear NAME:

This letter is in response to the complaint that you filed on January 1, 2024, with the Illinois Office of the Attorney General regarding collection of sales tax on certain items. The Office of the Attorney General forwarded your complaint to the Illinois Department of Revenue. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

NAME OF SELLER/PROVIDER OF SERVICE

COMPANY
ADDRESS1

COMPLAINT DESCRIPTION

The restaurant is charging a tip charge on top of my total bill, and taxing on the tip on the total bill. They claim its a service charge for parties of 3 or more but on the receipt it says tip and the tip was also taxed.

REQUESTED RELIEF

Some form of regulation as to not be taxed on mandatory tips.

NOTIFY BUSINESS

Please do not send this complaint to the business.

DEPARTMENT'S RESPONSE:

The Retailers' Occupation Tax Act imposes a tax upon persons engaged in this State in the business of selling tangible personal property at retail to purchasers for use or consumption. 35 ILCS 120/2. The Use Tax which complements the Retailers' Occupation Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. 35 ILCS 105/3. These taxes comprise what is commonly known as "sales tax" in Illinois. The information provided in this GIL is intended to provide you with the tax provisions relevant to your inquiry regarding the taxation of mandatory service charges.

The Retailers' Occupation Tax is measured by the gross receipts from sales of tangible personal property made in the course of business. See 86 Ill. Adm. Code 130.101. "Selling price" or the "amount of sale" means the consideration for a sale valued in money whether received in money...and shall be determined without any deduction on account of the cost of the property sold, the cost of materials used, labor or service cost or any other expense whatsoever...." 35 ILCS 120/1. The costs of doing business are an element of the retailer's gross receipts subject to tax, even if separately stated on the customer's bill. See 86 Ill. Adm. Code 130.140.

The tax does not apply to receipts from mandatory service charges that are separately stated on customers' bills to the extent that the proceeds of the service charge are in fact turned over to the employees as tips or as a substitute for tips to the employees who participate directly in preparing, serving, hosting, or cleaning up the food or beverage function with respect to which the service charge is imposed. See 86 Ill. Adm. Code 130.2145(d). However, to the extent that the service charges are used to fund or pay wages, labor costs, employee benefits, or employer costs of doing business, such charges are taxable gross receipts. See 86 Ill. Adm. Code 130.120(r); 86 Ill. Adm. Code 130.2145(d). Voluntary gratuities are not included in taxable gross receipts.

If the proceeds from mandatory service charges are not taxed, the retailer must show through its books and records that the gratuities are paid to the employees as a gratuity and not in the form of higher wages or used for other purposes. For example, if the retailer's payroll records show the proceeds from mandatory service charges are being paid to employees as wages rather than gratuities, then the mandatory gratuities will be subject to retailers' occupation tax.

All sales of tangible personal property are presumed subject to tax, and the burden of proving that a transaction is not taxable is upon the person who would be required to remit the tax to the Department if such transaction is taxable. See 86 Ill. Adm. Code 130.801(g)(2). A retailer's obligation to maintain books and records to support any claims of exemption from sales tax is governed by Section 7 of the

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Retailers' Occupation Tax Act, 35 ILCS 120/7. Retailers must maintain complete books and records which document, and clearly explain all the information regarding deductions as well as gross receipts required for tax returns. See 86 Ill. Adm. Code 130.801(b)-(c).

If the mandatory service charge described in your letter was treated by the retailer as a cost of doing business rather than as gratuities turned over as gratuities to its employees, the mandatory service charge would have been subject to retailers' occupation tax.

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Tom Grudichak
Associate Counsel

TG:sc