

INTERPRETATION NOTE: NO. 76

DATE: 26 February 2014

ACT : INCOME TAX ACT NO. 58 OF 1962
SECTION : SECTION 1(1), DEFINITION OF THE TERM “GROSS INCOME”
FOURTH SCHEDULE TO THE ACT, PARAGRAPH 1 DEFINITIONS: “REMUNERATION”, “EMPLOYER”, “EMPLOYEE”, “PROVISIONAL TAXPAYER”, PARAGRAPH 2(1)
SUBJECT : THE TAX TREATMENT OF TIPS FOR RECIPIENTS, EMPLOYERS AND PATRONS

CONTENTS

	PAGE
Preamble	2
1. Purpose.....	2
2. Background	3
2.1 The form of tips	3
2.2 The manner of payment or distribution	3
3. The law.....	5
4. Application of the law.....	5
4.1 The recipient.....	5
4.1.1 Gross income	5
(a) Any amount received by or accrued to.....	5
(b) In respect of services rendered.....	6
4.1.2 Provisional tax	8
4.2 The owner	9
4.2.1 Introduction	9
4.2.2 Obligation to withhold employees’ tax.....	9
(a) Remuneration.....	10
(b) Employee	11
(c) “Employer” as defined	11
(d) Owner’s, in a tripartite tipping relationship, obligation to withhold employees’ tax....	13
4.2.3 SDL.....	13
4.2.4 UIF	14
4.3 The patron.....	14
4.3.1 Introduction	14

4.3.2	Obligation to withhold employees' tax.....	14
4.3.3	SDL.....	16
4.3.4	UIF.....	17
5.	The bipartite position.....	17
6.	Conclusion.....	17
	Annexure A – The law.....	19
	Annexure B – Exemptions.....	22

Preamble

In this Note unless the context indicates otherwise –

- “**‘employer’ as defined**” means an “employer” as defined in paragraph 1;
- “**owner**” means a person who employs a recipient and pays the recipient a salary or wage, and potentially pays a tip in his or her own capacity or distributes tips paid by patrons to the recipient;
- “**paragraph**” means a paragraph of the Fourth Schedule to the Act;
- “**patron**” means a person, other than an owner, who awards a recipient a tip for services received;
- “**recipient**” means a person who receives a tip from a patron or owner for services rendered and includes, for example, waitrons, ushers, casino personnel, car guards, hotel personnel, petrol pump attendants, car guards, concierges, porters, tour guides, hairdressers, taxi drivers and car washers;
- “**SDL**” means the Skills Development Levy as levied under the Skills Development Levies Act No. 9 of 1999;
- “**section**” means a section of the Act;
- “**services rendered**” includes services rendered and services to be rendered;
- “**the Act**” means the Income Tax Act No. 58 of 1962;
- “**tip**” means a voluntary payment that is primarily awarded by a patron to a recipient who renders a service. The amount of the tip may be related to the quality of the service but it is also often awarded because of social custom or out of kindness;
- “**UIF**” means the Unemployment Insurance Fund contribution payable under the Unemployment Insurance Contributions Act No. 4 of 2002;
- “**waitron**” means a waiter or waitress; and
- any word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This Note discusses and clarifies the potential income tax, SDL and UIF implications for a recipient on the receipt of tips encountered in (but not limited to) the service industry. This Note will focus on a “tripartite” tipping relationship between the following three parties:

- The patron

- The recipient
- The owner

For example, a customer (the patron) pays a waitron (the recipient) a tip for excellent service in a restaurant owned and operated by the owner. In some circumstances, the owner may also pay the recipient a tip in the owner's own capacity.

This Note considers an employee's potential obligation to include the receipt of tips in gross income and that employee's related provisional tax and UIF responsibilities. It also considers the owner and a patron's possible obligations to withhold employees' tax on such tips and to account for SDL and UIF.

2. Background

2.1 The form of tips

Tips are generally awarded in money, for example, cash, cheque or by adding the tip to the total amount paid when making a credit or debit card payment. However, tips are not restricted solely to money and may take another form, for example, tickets to a sporting or entertainment event or, especially in the gambling industry, a casino chip or token.

2.2 The manner of payment or distribution

Tips may be paid directly by a patron to a recipient. For example, a patron gives a waitron a R50 note as a tip in recognition of the service rendered.

Alternatively, the patron may pay the tip to the owner. It is important to determine what role the owner is playing when receiving a tip from a patron, that is, whether the tip has been received by or accrued to the owner for the owner's own benefit (or potentially for the owner's own benefit) or, alternatively, whether the owner is purely acting as a conduit between the patron and the recipient of the tip.¹ In the role of a conduit, the owner is merely a channel which the patron is using, sometimes unknowingly, to transmit the tip to the recipient. The owner could either immediately distribute the tip to the employee in the form of cash, or the owner could distribute the tip later in, for example, cash or by depositing the amount into the recipient's bank account.

The facts and circumstances of each situation must be considered in determining the role the owner is playing. A unique feature to tips is that, although the patron's intentions are not disregarded, it is critically important to look at the arrangement for tips. The reason for this is because the arrangement will determine who is beneficially entitled to the tips and therefore whether the owner is acting as a conduit or as a receiver in his or her own right. For example, a patron may assume that the tip is being paid to the recipient, however, the recipient and the owner may have agreed that the owner will be entitled to all tips earned and that the employee will receive a higher hourly wage rate in view of this arrangement.

¹ Although not part of the subject matter of this Note, it is noted that in the conduit situation the tip is not received by the owner for his or her own benefit and does not form part of the owner's gross income. However, when the tip is received by the owner for the owner's own benefit it must be included in the owner's gross income.

An owner plays the role of a conduit if, for example –

- all tips (cash and non-cash) for a specific recipient are accumulated and subsequently paid by the owner to that recipient (for example, a patron adds 10% to his or her restaurant bill which is settled by credit card, and the owner subsequently pays that 10% to the waitron who served the patron); or
- all tips (cash and non-cash) for all recipients are collected (in what is often referred to as a “tipping pool”) and are subsequently distributed according to a pre-agreed formula to all recipients and possibly other employees who are part of the chain of service (for example, all tips are collected and subsequently distributed according to the following formula: 70% of the tips are distributed to waitrons based on the number of hours each waitron worked and 30% of the tips are distributed to the hostess, bartender and kitchen team based on the number of hours worked).

Examples of an owner not playing the role of a conduit and the tip being received by or accruing to the owner for the owner’s own benefit, include –

- all tips (cash and non-cash) are collected (in a tipping pool) and the owner has full authority to decide on the portion of the tipping pool which will be distributed to employees and the amount that a particular employee will receive; or
- the recipient and the owner agree in advance that the employee will receive a higher hourly wage rate and that the owner will be entitled to all tips earned.

The Note does not deal with compulsory service charges² (for example, adding a 10% service fee to a restaurant bill for tables exceeding eight guests), however for completeness it is noted that the facts and circumstances applicable to a compulsory service charge will determine whether the owner receives the service charge for the owner’s own benefit (often but not necessarily the case) or as a conduit on behalf the owner’s employees.

In summary:

- The recipient may therefore receive a tip from a patron, from the owner acting as a conduit for the patron or from the owner in the owner’s own capacity (which may be funded out of tips which were previously received by or accrued to the owner or from other sources). The income tax consequences for the recipient are discussed in **4.1**.
- The owner may receive the tip as a conduit and on-pay it to the recipient, or the owner may receive the tip for the owner’s own benefit.³ The owner’s potential employees’ tax, SDL and UIF obligations are discussed in **4.2**.
- The patron’s potential employees’ tax, SDL and UIF obligations are discussed in **4.3**.

² Refer definition of a “tip” which does not include a compulsory service charge.

³ Although not part of the subject matter of this Note, it is noted that in the conduit situation the tip is not received by the owner for his or her own benefit and is not part of the owner’s gross income. However, when the tip is received by the owner for the owner’s own benefit it must be included in the owner’s gross income.

3. The law

For ease of reference section 1(1) and the paragraphs of the Fourth Schedule used in this Note are quoted in **Annexure A**.

4. Application of the law

4.1 The recipient

From a recipient's perspective it is necessary to consider whether a tip which has been received by or accrued to him constitutes gross income. Gross income is a critical element of a taxpayer's taxable income calculation and has a direct impact on the amount of income tax payable.⁴ It is also necessary to consider whether the recipient has any provisional tax responsibilities. These aspects are discussed in **4.1.1** and **4.1.2**.

The applicable UIF responsibilities are dealt with in **4.2.4** and **4.3.4**.

4.1.1 Gross income

The term "gross income" is broadly defined in section 1(1) as the total amount, in cash or otherwise, received by or accrued to a resident during a year of assessment which is not of a capital nature. In addition, paragraph (c) of the definition of the term "gross income" specifically includes "any amount, including any voluntary award, received or accrued in respect of services rendered or to be rendered."

(a) Any amount received by or accrued to

The term "amount" is not defined in the Act. However, it has been the subject matter of various court cases and has been held to include money and receipts or accruals in a form other than money which have a monetary value.⁵

In *Geldenhuis v CIR* Steyn J stated that the words "received by" as used in the definition of the term "gross income" –⁶

"must mean 'received by the taxpayer on his own behalf for his own benefit'".

The term "accrued to" was held by Watermeyer J (as he then was) in *WH Lategan v CIR* to mean –⁷

"to which he has become entitled".

The facts of each case must be considered, however, in most cases these requirements will clearly be met because tips are generally awarded in cash so the amount is easily ascertainable and the timing of the receipt or accrual generally coincides with the clearly identifiable event of receiving the cash.

⁴ Section 5(1).

⁵ *C: SARS v Brummeria Renaissance (Pty) Ltd and Others* 2007 (6) SA 601 (SCA), 69 SATC 205; *CIR v Butcher Bros (Pty) Ltd* 13 SATC 21, 1945 AD 301; *WH Lategan v CIR* 2 SATC 16, 1926 CPD 203; *CIR v People's Stores (Walvis Bay) (Pty) Ltd* 52 SATC 9, 1990 (2) SA 353 (A).

⁶ 1947 (3) SA 256 (C), 14 SATC 419 at 430.

⁷ 1926 CPD 203, 2 SATC 16 at 20. The correctness of the interpretation of "accrued to" in *Lategan's* case was subsequently confirmed by Hefer JA in *CIR v People's Stores (Walvis Bay) (Pty) Ltd* 1990 (2) SA 353 (A), 52 SATC 9 at 24.

(b) In respect of services rendered

The courts⁸ have held that “in respect of” connotes a causal relationship between the amount received and, in context, the taxpayer’s service.

In the South African service industry it is a well-established practice and fact that recipients are often remunerated for the services rendered, firstly, by means of a basic salary or wage and, secondly, by means of tips paid by patrons. Recipients are very aware of the two sources of income and of the fact that the manner in which the recipient renders the service to the owner has a direct impact on patrons’ experiences and the amount of, if any, tips the recipients receive. The tips are worked for and are an expected source of income. The fact that the tip may be paid by a patron and not the owner does not alter the fact that there is a direct causal connection between the services rendered by the recipient and the tip received. The recipient’s services to the owner are the very reason or cause for the tips. There is no “independent, unconnected and extraneous causative factor or event”⁹ which isolates the tips from the services rendered by the recipient.

Accordingly, tips are received or accrue in respect of services rendered and fall within paragraph (c) of the definition of the term “gross income”.¹⁰

In the English case of *Calvert (Inspector of Taxes) v Wainwright*,¹¹ a taxi driver received a wage from his employer and tips from his passengers. Atkinson J held that:¹²

“Tips received by a man as a reward for services rendered, although voluntary gifts made by people other than his employers, are assessable to tax as part of the profits arising out of his employment if they are given in the ordinary way as a reward for services, but on the other hand, personal gifts, which means gifts to a man on personal grounds irrespective of and without regard to the question whether services have been rendered or not, are not assessable.”

The tips given to the taxi driver were held to be a reward for the services rendered and accordingly assessable to income tax.

In *Stander v CIR*¹³ the taxpayer was employed as a secretary and bookkeeper by Frank Vos Motors (a Delta franchise holder) and, in recognition of the meticulous manner in which he recorded data and prepared reports for Frank Vos Motors (which were submitted to Delta on a regular basis), Delta awarded him a prize. The court noted that:¹⁴

“The fact that Stander was an employee of Frank Vos Motors, was a *sine qua non* to his receiving the award. ... That fact does not, however, provide the necessary causal link between the services which he rendered to his employer and his obtaining of the award. Those services did not constitute the *causa causans* of the award. He did not

⁸ *Mariana Bosch, Brent James Curry, Ian Robert McClelland v CIR*, case 12760, 12828, 12756, Tax Court, 14 September 2011; ITC 1493 53 SATC 187; *Stevens v CSARS* 2007 (2) SA 554 (A); *Stander v CIR* 1997 (3) SA 617 (C); *De Villiers v CIR* 1929 AD 227.

⁹ *CIR v Shell Southern Africa Pension Fund* 46 SATC 1 at 9; 1984 (1) SA 672 (A).

¹⁰ For completeness it is noted that the facts in this paragraph are sufficient to meet the requirements of both the “basic” gross income definition and paragraph (c) of the definition of the term “gross income”.

¹¹ [1947] 1 All ER 282.

¹² At 282.

¹³ 59 SATC 212.

¹⁴ At 220 and 221.

seek the prize by entering a competition (*Cf ITC 976 24 SATC 812*) nor did he expect to receive anything from Delta for the work he performed for Frank Vos Motors. He merely performed his normal duties for which he was remunerated by his employer. The fact that these duties were performed in a manner which Delta considered to be excellent was what qualified him to receive the prize.

...

The fact that these services¹⁵ were beneficial to Delta does not mean that the award he received was 'in respect of' services rendered. The *sine qua non* referred to above does not provide the necessary causal link between what Stander did and the award he received.”

This case is, however, clearly distinguishable from the situation in which a recipient receives a tip from a patron for services rendered to the owner. Mr Stander was not aware of and did not work for the prize. It was a fortuitous receipt which the court held was causally linked to Delta's marketing management programme and Delta's decision to award prizes and not to Mr Stander's services. In contrast, recipients work for and expect tips in return for the service rendered hence the receipt of a tip is not fortuitous. In addition, the decision by the patron to give or not give the recipient a tip is not an independent and unconnected event which breaks the chain of causation. The decision is directly and integrally linked to the services rendered to the owner.

The recipient is required to declare all gross income received in the form of tips in the recipient's annual income tax return. Income tax will be payable by the recipient if taxable income exceeds the annual tax threshold.

Example 1 – Gross income

Facts:

A, aged 19, works as a porter for the Sparkling Waters Hotel Group in Port Elizabeth. A is required to assist hotel guests by collecting the guest's luggage on arrival and carrying it to the designated hotel room. A is also required to collect the guest's luggage and transfer it to the guest's vehicle upon departure from the hotel. For the 2013 year of assessment A received a gross salary of R42 000. In addition, A received tips amounting to R15 010 from guests for services rendered.

Result:

A must declare all income received or accrued for services rendered in the annual tax return, that is, A must include the salary income and the tips received from hotel guests.

A is not relieved of the requirement to declare both sources of income if A may ultimately not pay tax (for example, if the taxable income is below the annual threshold).

¹⁵ The services rendered to Frank Vos Motors.

Example 2 – Gross income*Facts:*

Z works as a waitron for Casino Groups Inc. Z is tasked with serving customers seated at the poker and blackjack gambling tables in the VIP Room. Z often receives generous tips from customers.

Casino Group Inc's policy is that employees may not report for duty with cash on their person without authorisation from senior management and having declared it to the Security Department. Tips received by employees must be declared and paid over to the Casino Cash Desk upon receipt of the tip.

Tips declared and paid over will be held in safe custody by the casino in the casino's bank account until transferred into the employees' bank accounts at month-end together with the employees' salaries. Employees whose services are terminated for any reason will receive their tips together with their last salary payment.

Casino Groups Inc. paid R28 252, consisting of a net salary of R9 840 and tips of R18 412, into Z's bank account on 25 August 2012. Z's gross salary was R15 100.

Result:

Z's gross salary of R15 100 and tips of R18 412 were received for services rendered and accordingly must be included in "gross income" under the paragraph (c) of the definition of the term "gross income".¹⁶ Gross income is a critical component of Z's taxable income calculation and the calculation of Z's normal tax liability.

Example 3 – Gross income*Facts:*

M, aged 20, is a student who earns money by working as a barman in one of the private suites at ABC Stadium operated by the XYZ Rugby Union. During June 2012, M received cash tips of R5 800 for services rendered. In addition, the suite lessee gave M two season tickets to the value of R2 000 as a tip in recognition of the excellent manner in which M took care of the lessee's guests.

Result:

M has received gross income in accordance with paragraph (c) of the definition of the term "gross income". M's income tax return must include the cash tips (R5 800) and the monetary value of the two season tickets (R2 000).

4.1.2 Provisional tax

Provisional taxpayers are required to make advance payments in respect of their liability for income tax in every year of assessment.

Subject to certain exemptions, a provisional taxpayer includes any person (other than a company) who derives income which does *not* constitute "remuneration" (as defined).¹⁷

¹⁶ Section 1(1).

¹⁷ Definition of a "provisional taxpayer" and the term "remuneration" in paragraph 1.

In most situations it is anticipated that tips will constitute remuneration, however, there are limited circumstances under which tips may not constitute remuneration. It is therefore critically important that the particular facts and circumstances are reviewed in determining whether or not the tips received constitute remuneration. See **4.2.2(a)** for a discussion on what constitutes remuneration and the criteria the recipient will need to consider in assessing whether a tip received is “remuneration” as defined.

The recipient will not have to register for provisional tax when the tip constitutes remuneration.¹⁸ This does *not* mean that the recipient will not have to pay income tax on the tips received. Income tax will be payable if the recipient’s taxable income calculation exceeds the tax threshold in a particular year and, if no provisional tax or employees’ tax payments have been made, the full amount of income tax will be payable by the recipient at the end of the year.

The recipient will have to register for provisional tax if the tip does not constitute remuneration and the recipient does not qualify for an exemption.¹⁹ The exemptions are discussed in **Annexure B**.

Refer to the *Reference Guide – Provisional Tax* on the SARS website www.sars.gov.za for additional information on provisional tax.

4.2 The owner

4.2.1 Introduction

As noted in **2.2**, an owner may receive the tip as a conduit and on-pay it to the recipient. Alternatively, an owner may receive the tip for the owner’s own benefit and subsequently pay a recipient a tip in his or her own capacity from his or her own resources.

The owner’s involvement in paying the tip may have employees’ tax consequences for the owner – see **4.2.2**. The owner may also have SDL and UIF obligations – see **4.2.3** and **4.2.4**.

4.2.2 Obligation to withhold employees’ tax

Paragraph 2(1) requires that every resident “employer” as defined or representative employer who pays or becomes liable to pay any amount by way of *remuneration* to any *employee* shall, unless the Commissioner has granted authority to the contrary, deduct or withhold employees’ tax²⁰ from that amount and pay it over to the Commissioner.

There are three main elements that must be met before an owner is obliged to deduct or withhold employees’ tax, namely –

- remuneration;
- employee; and
- “employer” as defined.

¹⁸ Assuming the recipient is not (and is not required) to be registered for reasons other than the receipt or accrual of tips.

¹⁹ Assuming for the moment that the recipient is not already registered for provisional tax for other reasons.

²⁰ As calculated under the Fourth Schedule.

Each of these elements will be examined in the context of a tripartite tipping relationship (see **4.2.2(a) – 4.2.2(c)**) before considering whether it means an owner in a tripartite tipping relationship is required to withhold employees' tax (see **4.2.2(d)**).

(a) Remuneration

The term “remuneration” is defined in paragraph 1 as –

“any amount of income which is paid or is payable to any person by way of any salary, leave pay, wage, overtime pay, bonus, gratuity, commission.... whether in cash or otherwise and whether or not in respect of services rendered, including—

- (a) any amount referred to in paragraph (c) of the definition of “gross income” in section 1(1)...

but not including—

...

- (ii) any amount paid or payable in respect of services rendered or to be rendered by any person in the course of any trade carried on by him independently of the person by whom such amount is paid or payable and of the person to whom such services have been or are to be rendered: Provided ...”.

(Emphasis added)

The proviso to subparagraph (ii) contains statutory tests which, if met, override the factual position and deem a person not to carry on a trade independently for employees' tax purposes.

As discussed in **4.1.1(b)** tips fall within paragraph (c) of the definition of the term “gross income” and accordingly, initially at least, are included in “remuneration” as defined. It is then necessary to determine whether the subparagraph (ii) exclusion of the remuneration definition applies. Amounts are excluded from remuneration if received from an independent trade. Technically, the common law tests should be applied first to determine whether the amount was received in the course of carrying on an independent trade and, if the answer is in the affirmative, then the statutory tests in the proviso would be applied to determine whether, irrespective of having met the common law tests, the person is deemed not to be carrying on an independent trade. However, in practice the statutory tests are often considered first and, only if the statutory tests are not applicable in a particular situation, are the common law tests applied to determine whether the person is indeed carrying on an independent trade. In this Note, the statutory tests are considered first.

The statutory tests²¹ provide that –

- if the services are required to be performed mainly at the premises of the person –
 - by whom the amount is paid or payable; or
 - to whom such services are rendered or will be rendered; and
- the person rendering the services is subject to the control or supervision of any other person as to the –
 - manner in which the person's services are or will be performed, or

²¹ Proviso to subparagraph (ii) of the definition of the term “remuneration” in paragraph 1.

- the hours of that person's work,

then the person is deemed not to carry on an independent trade and the amount so received or receivable is not, therefore, excluded from remuneration.

The facts and circumstances of each case will need to be considered in determining whether the statutory tests are met. For example, if a recipient only works at the owner's restaurant premises then the statutory test is likely to be met because the services are mainly performed at the premises of the person to whom such services are rendered (see **4.1.1(b)** for a discussion on whom the recipient renders services to) and it is likely that person will also control the recipient's hours or supervise the manner in which the services are performed. In these circumstances, one of the statutory tests will be met and tips will constitute remuneration.

In contrast, if, for example, the recipient only delivers take-away orders for the restaurant then based on the detailed facts it may be that the recipient's services are not mainly performed at the restaurant owner's premises and, given that the services are almost certainly not performed at the customer's premises (who would most likely be awarding the tip), it means that none of the statutory tests will be met.

In the event that none of the statutory tests is met, it is necessary to determine whether or not the recipient rendered the services as part of an independent trade. The appropriate common law tests²² must be applied in making this determination. Tips will not constitute "remuneration" as defined if the services to which the tips relate are rendered by the recipient as part of an independent trade (remembering this is premised on the basis that none of the statutory tests applied). Tips will constitute "remuneration" as defined if an independent trade *is not* being conducted.

See **Example 4**.

(b) Employee

An "employee" is defined²³ as, amongst others, any person (other than a company) who receives any amount of remuneration or to whom any remuneration accrues.

A recipient will constitute an "employee" as defined if the tip the recipient receives for services rendered constitutes remuneration. As seen in **4.2.2(a)**, whether or not the tip constitutes "remuneration" as defined will depend on the facts and circumstances of each case. (See **Example 4**.)

(c) "Employer" as defined

It is important to determine whether an owner meets the definition of an "employer" as defined. An "employer" is defined in paragraph 1 as, amongst others, –

"any person (excluding any person not acting as a principal, but including any person acting in a fiduciary capacity or ...) who pays or is liable to pay to any person (*in context the recipient*) any amount by way of remuneration, ...".

(Emphasis added)

As noted in **4.2.2(a)**, whether or not a tip constitutes remuneration will depend on the facts of the particular case. For the purposes of determining whether an owner is an

²² See Interpretation Note No. 17 (Issue 3) dated 31 March 2010 "Employees' Tax: Independent Contractors".

²³ Paragraph 1, paragraph (a) of the definition of an "employee".

“employer” as defined, this section (that is, **4.2.2(c)**) assumes that the tip constitutes remuneration and considers two situations.

The two situations considered are, firstly, the owner acting as conduit and secondly the owner receiving the tip for the owner’s own benefit and subsequently deciding to pay the recipient a tip in his or her own capacity. The detailed facts and circumstances of each case must be considered in determining which situation is applicable in a particular case.

In context it is necessary to consider whether the owner in each of these situations is acting as a principal or as a fiduciary.

The words “principal” and “fiduciary” are not defined in the Act and should be interpreted according to the ordinary meanings as applied to the subject matter with regard to which it is used.

A “principal” is defined in the Merriam-Webster Online Dictionary,²⁴ as –

“a person who has controlling authority or is in a leading position: as a :

- a) A chief or head man or woman
- b) ...
- c) one who engages another to act as an agent subject to general control and instruction; specifically : the person from whom an agent's authority derives
- d) ...
- e) the person primarily or ultimately liable on a legal obligation
- f) ...”.

The Free Dictionary Online²⁵ defines “fiduciary” as:

“a person to whom property or power is entrusted for the benefit of another.”

In the context of the Fourth Schedule, and applying the dictionary definitions of a principal and a fiduciary, it is clear that when acting as a conduit (see examples in **2.2**) the owner is not acting as a principal or a fiduciary. In the role of a conduit the owner has no controlling authority in relation to the payment of or the amount of the tip and there is no responsibility or obligation on the owner to manage the tip for the benefit of the recipient. The owner is merely temporarily holding the funds for the recipient (that is, has physical custody of the funds) and performing a distribution role for the patron. Accordingly, in these circumstances the employer would not constitute an “employer” as defined for purposes of employees’ tax.

The position is different if the owner receives the tip for the owner’s own benefit (see examples in **2.2**) and subsequently decides to pay the recipient a tip in his or her own capacity as owner. The owner is still not acting as a fiduciary because the tip has been received for the owner’s own benefit and is not being, nor is there any requirement for it to be, managed or controlled by the owner for the benefit of the recipient. However, when subsequently paying the recipient the tip the owner is acting as a principal because the owner is acting in his or her own capacity and has exercised his or her own controlling authority in deciding firstly to pay the recipient a tip and secondly in deciding on the amount of the tip. Accordingly, in this circumstance the owner would constitute an “*employer*” as defined for employees’ tax purposes (assuming the remuneration element is met – see **4.2.2(a)**).

²⁴ www.merriam-webster.com/dictionary/principal [Accessed 25 February 2014].

²⁵ www.thefreedictionary.com/fiduciary [Accessed 25 February 2014].

See **Example 4**.

(d) Owner's, in a tripartite tipping relationship, obligation to withhold employees' tax

As discussed above, there are three main elements (remuneration, employee and "employer" as defined) that must be met before an owner is obliged to deduct or withhold employees' tax.

An owner who is acting as a conduit will not be an "employer" as defined (see **4.2.2(c)**) and, accordingly, the owner will not be required to withhold employees' tax from tips paid over to the recipient on behalf of the patron.

In contrast, if the owner has received the tip for the owner's own benefit and subsequently decides to pay a recipient a tip, the obligation to withhold employees' tax will depend on whether or not the tip constitutes remuneration. This will depend on the facts and circumstances of each case (see **4.2.2(a)**) but assuming the tip constitutes remuneration, which it often will, the owner will be required to withhold employees' tax as under the circumstances the owner will be an "employer" as defined (see **4.2.2(c)**) who is paying an employee (see **4.2.2(b)**) an amount of remuneration. No employees' tax must be withheld if the tip does not constitute remuneration.

See **Example 4**.

4.2.3 SDL

The Skills Development Levies Act No. 9 of 1999 provides that every employer must pay SDL at a rate of 1% of the leviable amount.

The leviable amount is based on the definition of the term "remuneration" in the Fourth Schedule. There are certain exclusions to the leviable amount which are not applicable to tips.

An "employer" is defined in the Skills Development Levies Act as including "an employer as defined in the Fourth Schedule to the Income Tax Act".

An owner who pays a tip to a recipient in the role of a conduit is not an "employer" as defined in the Fourth Schedule (see **4.2.2(c)**). The word "includes" is not exhaustive, however, SARS accepts that in the context of tips and SDL, an owner acting in the role of a conduit will not be acting as an "employer" as defined and will not be required to include any tips paid as a conduit in the leviable amount.

An owner who pays a tip to a recipient in the owner's own capacity will be an "employer" as defined in the Fourth Schedule (see **4.2.2(c)**). Accordingly, if that tip also constitutes remuneration it must be included in the leviable amount for SDL purposes.

Refer to the *Guide for Employers in respect of the Skills Development Levy* on the SARS website www.sars.gov.za for general information on the SDL.

4.2.4 UIF

The Unemployment Insurance Contributions Act No. 4 of 2002 provides that “every employer and every employee to whom this Act applies must, on a monthly basis, contribute to the Unemployment Insurance Fund”.²⁶ It applies to all employers and employees other than, amongst others specifically detailed in this Act, an employee and his or her employer when the employee is employed by that employer for less than 24 hours a month.

The amount of the contribution payable –²⁷

- by an employee, must be 1% of the remuneration paid to that employee by his or her employer; and
- by an employer for any one of its employees, must be equal to 1% of the remuneration paid to that employee.

An “employer” is defined in the Unemployment Insurance Contributions Act as meaning an “employer” as defined in paragraph 1 of the Fourth Schedule.

An owner who pays a tip to a recipient in the role of a conduit is not an “employer” as defined in the Fourth Schedule (see **4.2.2(c)**) and accordingly is not required to contribute to the Unemployment Insurance Fund. Furthermore, because the amount is being paid by the owner as a conduit and not as an “employer” as defined, the owner is not required to withhold UIF on behalf of the recipient.

An owner who pays a tip to a recipient in the owner's own capacity will be an “employer” as defined in the Fourth Schedule (see **4.2.2(c)**). Accordingly, if that tip also constitutes remuneration (see **4.2.2(a)**) it must be included in the calculation of the amount of the owner's UIF contribution and the employee's UIF contribution (which the owner must withhold and pay over on behalf of the recipient). No UIF contribution is required if the tip does not constitute remuneration.

Refer to the *Guide for Employers in respect of the Unemployment Insurance Fund* on the SARS website www.sars.gov.za for general information on UIF.

4.3 The patron

4.3.1 Introduction

The payment of a tip by a patron may give rise to employees' tax, SDL and UIF obligations for that patron. These potential consequences are dealt with in **4.3.2**, **4.3.3** and **4.3.4** respectively.

4.3.2 Obligation to withhold employees' tax

Consistent with the position of the owner as discussed in **4.2.2**, a patron will *prima facie* be required to withhold employees' tax from the tip paid to a recipient if the following three main elements are met:

- Remuneration – whether or not the tip that the patron gives the recipient constitutes remuneration will depend on the facts and circumstances of the particular case (see **4.2.2(a)** – equally applicable to the owner and the patron).

²⁶ Section 5 of the Unemployment Insurance Contributions Act, 2002.

²⁷ Section 6 of the Unemployment Insurance Contributions Act, 2002.

- Employee – the recipient will be an “employee” as defined if the tip constitutes remuneration (see **4.2.2(b)** – equally applicable to the owner and the patron).
- “Employer” as defined – the patron is clearly exercising his or her own authority and acting as a principal when paying the recipient a tip and will therefore be an “employer” as defined if the tip constitutes remuneration (see **4.2.2(c)** for the definition of an “employer” as defined and a discussion of the definition and its component parts).

Accordingly, if the tip constitutes remuneration (this is dependant of the facts and circumstances of each case but in most situations a tip will constitute remuneration) the patron must *prima facie* withhold employees’ tax on tips paid to a recipient.

However, due to various practical constraints, by virtue of the authority exercised by the Commissioner in paragraph 2(1), the patron will not be required to withhold employees’ tax on tips paid to the recipient.

Example 4 – Gross income and employees’ tax

Facts:

N, aged 22, is employed full-time as a waitron by Succulent Burger Ranch in Rustenburg. For the week ending 2 September 2012, N received wages of R1 000 from the Succulent Burger Ranch.

The tipping agreement provides that all cash tips must be paid over to the Succulent Burger Ranch and included in the tipping pool and that all tips from patrons will be distributed among the waitrons based on the number of hours worked. The Succulent Burger Ranch automatically adds non-cash tips to the tipping pool. In addition to the R1 000 wages, N received R1 920 in tips from the tipping pool.

Result:

N

The wages of R1 000 and the tips of R1 920 are included in “gross income” by virtue of paragraph (c) of the definition of the term “gross income”. N’s income tax return must reflect both amounts.

Succulent Burger Ranch

Succulent Burger Ranch must withhold employees’ tax from the **wages** paid to N as the three elements are met:

- a) Remuneration – the wages constitute “remuneration” as defined in the Fourth Schedule as the wages were received by N in respect of services rendered and at least one of the statutory tests (see **4.2.2(a)**) are met as the services are only performed at the premises that Succulent Burger Ranch leases and Succulent Burger Ranch controls the hours and the manner in which N works.
- b) Employee – N has received remuneration of R1 000 (see **4.2.2(b)**). N is accordingly an “employee” as defined.
- c) “Employer” as defined – Succulent Burger Ranch is an “employer” as defined in relation to the R1 000 wages because the wages constitute remuneration and Succulent Burger Ranch is acting as a principal when it pays or is liable to pay N’s wages (see **4.2.2(c)**).

Succulent Burger Ranch must not withhold employees' tax from the **tips** as only two of the three elements are met (see **4.2.2(d)**):

- d) Remuneration – the tips constitute “remuneration” as defined in the Fourth Schedule as the tips were received by N in respect of services rendered and at least one of the statutory tests (see **4.2.2(a)**) are met as the services are only performed at the premises that Succulent Burger Ranch leases and Succulent Burger Ranch controls the hours and the manner in which N works.
- e) Employee – N has received remuneration of R1 920 (see **4.2.2(a)**). N is accordingly an “employee” as defined.
- f) “Employer” as defined – Succulent Burger Ranch is not an “employer” as defined because, although the tips are remuneration, Succulent Burger Ranch is acting as a conduit and not as a principal when paying or being liable to pay the tips to N (see **4.2.2(c)**).

Patron

Although the three elements for withholding tax are met in relation to a patron who gives N a tip (remuneration – refer reasons above, employee – refer reasons above, “employer” as defined – refer reasons above except that the patron is acting in his or her own capacity when paying a tip), by virtue of the authority in paragraph 2(1) the patron is not required to withhold employees' tax from tips given (see **4.3.2**).

4.3.3 SDL

As noted in **4.2.3**, every “employer” as defined in the Fourth Schedule must pay SDL at a rate of 1% of the leviable amount.

The leviable amount is the total amount of remuneration, paid or payable, by an employer to its employees during any month, as determined in accordance with the provisions of the Fourth Schedule, *for the purposes of determining the employer's liability for any employees' tax under that Schedule*, whether or not such employer is liable to deduct or withhold such employees' tax.²⁸

Although the patron is an “employer” as defined and the tip is remuneration as defined, the patron is not required to deduct or withhold employees' tax from the tip by virtue of the authority in paragraph 2(1) (see **4.3.2**). The patron is therefore not required to determine the amount of remuneration “*for purposes of determining the employer's liability for employees' tax*” because, by virtue of the authority under paragraph 2(1), the patron is not liable to withhold employees' tax and hence the leviable amount on tips would be nil.

Refer to the *Guide for Employers in respect of the Skills Development Levy* on the SARS website **www.sars.gov.za** for general information on the skills development levy.

²⁸ This means that the remuneration paid to employees below the income tax threshold must be incorporated into remuneration for determining the leviable amount in the Skills Development Act, 1999.

4.3.4 UIF

As noted in 4.2.4, the Unemployment Insurance Contributions Act applies to all employers and employees other than, amongst others as specifically detailed in this Act, an employee and his or her employer when the employee is employed by that employer for less than 24 hours a month.²⁹ By implication, it does not therefore apply when an employee is not actually employed by a party meeting the definition of an “employer”.

In a tripartite tipping relationship, although the patron is an “employer” as defined (see 4.3.2), the recipient has not been employed by the patron.³⁰ The patron is in effect paying the tip to the recipient for services rendered by the recipient to the owner (see 4.1.1(b)). Accordingly, there are no UIF obligations for the recipient or the patron in relation to tips paid by the patron.

Refer to the *Guide for Employers in respect of the Unemployment Insurance Fund* on the SARS website www.sars.gov.za for general information on UIF.

5. The bipartite position

This Note has discussed the income tax, SDL and UIF consequences in a tripartite tipping relationship. A bipartite tipping relationship exists when a recipient is not employed by an owner and there are only two parties, namely, the recipient and the patron. For example, a car guard who is self-employed and operates on his or her own receives a tip from a patron for looking after the patron’s car.

The consequences for the recipient and the patron in a bipartite tipping relationship are the same as those set out in 4.1 and 4.3 respectively.

6. Conclusion

Recipient

Tips received by or accrued to a recipient must be included in the recipient’s “gross income” by virtue of paragraph (c) of the definition of the term “gross income”. The recipient must declare the total amount of tips received to SARS in the recipient’s annual tax return.

The facts and circumstances of a particular recipient’s case will determine whether or not the tips are regarded as “remuneration” as defined. It is anticipated that in most situations tips will constitute “remuneration” as defined and the recipient will therefore not be required to register for provisional tax. If the tip does not constitute remuneration, the recipient may be required to register for provisional tax if he or she does not qualify for one of the exemptions as set out in **Annexure B**.

Owner

An owner may be acting as conduit for a patron or in the owner’s own capacity when paying a recipient a tip. In both instances the owner must consider his or her employees’ tax, UIF and SDL obligations.

²⁹ Section 4(1)(a) of the Unemployment Insurance Contributions Act, 2002.

³⁰ In any event, even if it could be said that the patron has employed the recipient, which is not the case, the period of employment for the particular recipient would be less than 24 hours per month.

An owner who is acting as a conduit will not be required to withhold employees' tax from the tips paid over to the recipient on behalf of the patron. The owner will also not be required to include the tips paid as a conduit in the leviable amount for SDL purposes or to make or withhold any contribution for UIF.

If the owner has received the tip for his or her own benefit and subsequently decides to pay a recipient a tip in his or her own capacity, the obligation to withhold employees' tax will depend on whether or not the tip constitutes remuneration. Assuming the tip constitutes remuneration, the owner will be required to withhold employees' tax. The owner will also be required to include the tip in the leviable amount for SDL purposes and to make a UIF contribution as well as withhold the recipient's UIF contribution. In contrast, if the tip does not constitute remuneration, no employees' tax must be withheld. The owner will also not be required to include the tip in the leviable amount for SDL purposes or to make or withhold any contribution for UIF.

Patron

A patron will not be required to withhold employees' tax from tips paid to a recipient. The patron is furthermore not required to include the tips paid in the leviable amount for SDL purposes or to make or withhold any contribution for UIF.

Annexure A – The law

Definition of the term “gross income” in section 1(1)

“gross income”, in relation to any year or period of assessment, means—

- (i) in the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident; or
- (ii) in the case of any person other than a resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such person from a source within the Republic,

during such year or period of assessment, excluding receipts or accruals of a capital nature, but including, without in any way limiting the scope of this definition, such amounts (whether of a capital nature or not) so received or accrued as are described hereunder, namely—

- (a)
- (b)
- (c) any amount, including any voluntary award, received or accrued in respect of services rendered or to be rendered or any amount (other than an amount referred to in section 8(1)) received or accrued in respect of any employment or the holding of any office: Provided that—
 - (i) the provisions of this paragraph shall not apply in respect of any benefit or advantage in respect of which the provisions of paragraph (i) apply;
 - (ii) any amount received by or accrued to or for the benefit of any person in respect of services rendered or to be rendered by any other person shall for the purposes of this definition be deemed to have been received by or to have accrued to the said other person;
 - (iii) to (vi) inclusive

Definition of the term “remuneration” in paragraph 1

“remuneration” means any amount of income which is paid or is payable to any person by way of any salary, leave pay, wage, overtime pay, bonus, gratuity, commission, fee, emolument, pension, superannuation allowance, retiring allowance or stipend, whether in cash or otherwise and whether or not in respect of services rendered, including—

- (a) any amount referred to in paragraph (a), (c), (cA), (d), (e), (eA) or (f) of the definition of “gross income” in section 1 of this Act;
- (b) – (f)

but not including—

- (i)
- (ii) any amount paid or payable in respect of services rendered or to be rendered by any person (other than a person who is not a resident or an employee contemplated in paragraph (b), (c), (d), (e) or (f) of the definition of “employee”) in the course of any trade carried on by him independently of the person by whom such amount is paid or payable and of the person to whom such services have been or are to be rendered: Provided that for the purposes of this paragraph a person shall not be deemed to carry on a trade independently as aforesaid if the services are required to be performed mainly at the premises of the person by whom such amount is paid or payable or of the person to whom such services were or are to be rendered and the person who rendered or will render the services is subject to the control or supervision of any other person as to the manner in which his or her duties are performed or to be performed or as to his hours of work: Provided further that a person will be deemed to be carrying on a trade independently as aforesaid if he throughout the year of assessment employs three or more employees who are on a full time basis engaged in the business of such person of rendering any such service, other than any employee who is a connected person in relation to such person;

The definition of an “employee” in paragraph 1

“employee” means—

- (a) any person (other than a company) who receives any remuneration or to whom any remuneration accrues;
- (b) any person who receives any remuneration or to whom any remuneration accrues by reason of any services rendered by such person to or on behalf of a labour broker;

.....

The definition of an “employer” in paragraph 1

“employer” means any person (excluding any person not acting as a principal, but including any person acting in a fiduciary capacity or in his capacity as a trustee in an insolvent estate, an executor or an administrator of a benefit fund, pension fund, pension preservation fund, provident fund, provident preservation fund, retirement annuity fund or any other fund) who pays or is liable to pay to any person any amount by way of remuneration, and any person responsible for the payment of any amount by way of remuneration to any person under the provisions of any law or out of public funds (including the funds of any provincial council or any administration or undertaking of the State) or out of funds voted by Parliament or a provincial council;

The definition of a “provisional taxpayer” in paragraph 1, read with paragraph 18

“provisional taxpayer” means—

- (a) any person (other than a company) who derives by way of income any amount which does not constitute remuneration or an allowance or advance contemplated in section 8(1);
- (b) any company; and
- (c) any person who is notified by the Commissioner that he or she is a provisional taxpayer,

but shall exclude—

- (aa) any public benefit organisation as contemplated in paragraph (a) of the definition of “public benefit organisation” in section 30(1) that has been approved by the Commissioner in terms of section 30(3);
- (bb) any recreational club as contemplated in the definition of “recreational club” in section 30A(1) that has been approved by the Commissioner in terms of section 30A(2); and
- (cc) any body corporate, share block company or association of persons contemplated in section 10(1)(e);
- (dd) a person exempt from payment of provisional tax in terms of paragraph 18.

Exemptions – paragraph 18

18. (1) There shall be exempt from payment of provisional tax—

- (a)
- (b) any person in respect of whose liability for normal tax for the relevant year of assessment payments are required to be made under section thirty-three of this Act;
- (c) any natural person who on the last day of that year will be below the age of 65 years and who does not derive any income from the carrying on of any business, if—
 - (i) the taxable income of that person for the relevant year of assessment will not exceed the tax threshold; or

- (ii) the taxable income of that person for the relevant year of assessment which is derived from interest, foreign dividends and rental from the letting of fixed property will not exceed R20 000;
 - (d) any natural person who on the last day of the year of assessment will be 65 years or older, if the Commissioner is satisfied that such person's taxable income for that year—
 - (i) will not exceed R120 000;
 - (ii) will not be derived wholly or in part from the carrying on of any business; and
 - (iii) will not be derived otherwise than from remuneration, interest, foreign dividends, or rental from the letting of fixed property.
- (2)

Paragraph 2(1) of the Fourth Schedule

2. (1) Every—

- (a) employer who is a resident; or
- (b) representative employer in the case of any employer who is not a resident,

(whether or not registered as an employer under paragraph 15) who pays or becomes liable to pay any amount by way of remuneration to any employee shall, unless the Commissioner has granted authority to the contrary, deduct or withhold from that amount, or, where that amount constitutes any lump sum contemplated in paragraph 2(1)(b) of the Second Schedule, deduct from the employees benefit or minimum individual reserve as contemplated in that paragraph, by way of employees' tax an amount which shall be determined as provided in paragraph 9, 10, 11 or 12, whichever is applicable, in respect of the liability for normal tax of that employee, or, if such remuneration is paid or payable to an employee who is married and such remuneration is under the provisions of section 7(2) of this Act deemed to be income of the employee's spouse, in respect of such liability of that spouse, and shall, subject to the Employment Tax Incentive Act, 2013, pay the amount so deducted or withheld to the Commissioner within seven days after the end of the month during which the amount was deducted or withheld, or in the case of a person who ceases to be an employer before the end of such month, within seven days after the day on which that person ceased to be an employer, or in either case within such further period as the Commissioner may approve.

Annexure B – Exemptions

See 4.1.2 – A recipient will have to register for provisional tax if the tips received do not constitute remuneration and the recipient does not qualify for an exemption from the requirement to register for provisional tax.

The exemptions applicable to natural persons vary depending on whether the person will be younger than 65 years on the last day of the year of assessment or 65 years and older on that day. A natural person who is younger than 65 and who does not derive any income from the carrying on of any business will be exempt if –

- his taxable income for that year will not exceed the tax threshold;³¹ or
- his taxable income for that year which is derived from interest, foreign dividends and rental from the letting of fixed property will not exceed R20 000.

Accordingly, if the tip is not “remuneration” as defined and the person is younger than 65, that person will need to consider the particular facts and circumstances to determine whether or not he or she is required to register for provisional tax.

A natural person (other than a director of a private company) who is 65 or older will be exempt if the Commissioner is satisfied that that person’s taxable income for that year –

- will not exceed R120 000;
- will not be derived wholly or in part from the carrying on of any business; and
- will not be derived otherwise than from remuneration, interest, foreign dividends, or rental from the letting of fixed property.

The last requirement will not be met if the tips are not “remuneration” as defined which means that a natural person who is 65 or older would need to register for provisional tax if the tips received do not constitute remuneration.

³¹ The amount of the tax threshold varies each year depending on the marginal tax rates and the rebates available.