

# When are Employee Tips Pensionable and Insurable?



## **SITUATION**

Cydnee Crosby is a waitress at the Hat Trick Cafe who earns tips. She receives her tip money in different ways. Her tips include:

- The cash customers leave on the table after the meal;
- The money customers add to their bill as a tip when they pay for the meal by credit card which the restaurant then pays to Cydnee in cash;
- The mandatory 18% service charge that the restaurant adds to the bills of tables of parties containing six persons or more; and
- A 10% share of the combined bar and coat check tips that the restaurant collects, pools and distributes according to a formula set by the employees themselves.

## **QUESTION**

**From which, if any, of the tips that Cydnee receives must the restaurant make source deductions for EI and CPP?**

- A) The cash tips that customers leave on the table.
- B) The tips that customers leave on their credit cards and that are paid to Cydnee, dollar for dollar, by the restaurant.
- C) The proceeds of the 18% service charge.
- D) The 10% of the tips that Cydnee receives from the pool.

[learn\_more caption="Click for Answer"]

## **ANSWER**

**C. Of the tips Cydnee receives, only the 18% service charge are pensionable under CPP and insurable under EI.**

## **EXPLANATION**

The tips and gratuities that an employee receives are taxable income under the *Income Tax Act*. But are they also insurable and pensionable income under EI and CPP,

respectively? The Rule of Thumb: Employers must make EI and CPP source deductions on tips only when they exercise “control” over the money. By contrast, tips paid directly by customers to the employee aren’t subject to EI and CPP source deductions. This scenario illustrates how the CRA and the courts apply this rule to common tip arrangements and is based on recent CRA guidance.

Three of the four arrangements described above would be considered direct tips. The only tips that Cydnee receives that the restaurant controls are the proceeds of the mandatory service charge that the restaurant adds to the bills of large parties. The restaurant has control not simply because it collects the money and pays the proceeds to Cydnee but because it sets the charge amount. This constitutes control making the money subject to EI and CPP source deductions.

#### **WHY WRONG ANSWERS ARE WRONG**

**A is wrong** because the cash that customers leave on tables or hand directly to employees is a form of direct tip. So it wouldn’t be fair to expect employers to account for and make EI and CPP deductions on this money.

**B is wrong** because even though the restaurant collects the money and transmits it to Cydnee, it pays her the specific amount that the customer lists. Because it doesn’t determine the credit card tip amount, the restaurant is serving as a conduit between the customer and Cydnee.

**D is wrong** because the restaurant is again acting as a conduit. If the restaurant determined the formula for distributing the money in the pool, it would likely be considered to have control over the tips. But it’s the employees who decide what percentage of the money each participant in the pool gets. So while the restaurant collects the money, puts it into a pool and distributes it to the employees, it’s not exercising control over the money in the pool and doesn’t have to make EI and CPP source deductions on it.