



## Good practice principles

Tips, service charges & tronc systems





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## About WMT

WMT Troncmaster Service Ltd advises on the set-up and management of ethical, fair and compliant tronc systems for hospitality businesses.

WMT Troncmaster Services Ltd is a member of the WMT Group.

The WMT Group is a group of accountants, business advisers and tax specialists that help business owners, private individuals and trustees achieve their goals. The Group has particular expertise in hospitality, property, professional services and charities sectors.

# ABOUT THIS GUIDE

**This guide is written for businesses in the hospitality sector whose customers choose to make payments of tips, gratuities and discretionary service charges. It is also intended to be an explanation of best practice for hospitality businesses, their employees and customers**

The principles outlined in this guide aim to promote transparency, understanding and good practice within the hospitality sector regarding discretionary and voluntary payments that customers may choose to make in respect of their experience.

Throughout this guide, the principles reflect the policy objectives set out by the Government in their 2016 consultation into tips, gratuities and services charges, namely that:

- it is clear to customers that the payments they are making are voluntary
- the voluntary payments made are received by workers
- the way payments are treated is clear and transparent to consumers and workers

Furthermore, these principles seek to ensure that, when discretionary voluntary payments are distributed to staff:

- everyone who contributed to the customer's experience receives a share;
- the distribution is calculated and managed fairly, independently of the employer, impartially and transparently;
- that staff feel rewarded, recognised and motivated; and
- that customers feel confident, when making such discretionary payments, that they are rewarding the team who have contributed to their experience.

The Government has stated it believes that tips and service charges should be dealt with through a "well managed" tronc system, and this document sets out best practice for running such a system.

The way in which gratuities are paid by customers, handled by a business, divided between the team, and paid to individual staff members will vary from business to business. This guidance is not intended to micro-manage or be prescriptive, but instead to offer a set of principles and standards to be used by businesses.

## **Other sources of information**

This guide is not intended to be a comprehensive statement of law nor a detailed guide to the taxation and employment legislation and regulations which businesses must follow when dealing with payments made by customers. The 2018 "Tips, Gratuities, Service Charges & Troncs – A Practical Guide for the UK Hospitality Industry", published by HOSPA, provides comprehensive guidance on the relevant legislation and taxation treatment.







# SUMMARY OF THE MAIN PRINCIPLES

This guide reflects what is widely accepted as good practice for the distribution of discretionary payments, as well as how they can be handled legally, fairly, transparently and ethically. For convenience, the main principles are summarised below.

Any tips or service charges paid by customers should be managed and processed in a way that is **fair and transparent**.

- Any **service charge** which the customer is invited to pay is always discretionary and should be clearly advertised as such.
- If customers are invited to pay for service, the business should operate **a fair and well-managed tronc system**.
- Customers expect **service charges to be paid to staff in addition to salaries or basic pay**, not as part of contractual agreements or obligations.
- The tronc system should seek to reward and benefit **all members of staff who contribute to the customer experience** and who deliver the service to consumers.
- **Businesses should generally not get involved in cash tipping**. Whatever cash staff receive directly from customers belongs to them.
- Businesses should ensure that **staff are aware of their legal obligations** to record and declare any cash tips to HMRC.
- The costs of collecting, processing, administering and distributing tips and service charge to staff (collectively known as administration costs), **generally these do not exceed 5% of the tips and service charge collected**. With the exception of these costs, businesses should make 100% of the funds available to the tronc system to allocate to the members.
- **Customers and staff should be clearly advised** of whether a tronc system exists, who manages it (a member of staff or an independent third party), and which groups of staff receive a share.
- **Staff should be made aware** of the rules of the tronc scheme, how their own share is calculated (e.g. points, minimum rates, equal share), the identity of the Troncmaster, and how to raise or ask questions regarding the operation of their scheme.
- The Troncmaster should **manage the tronc scheme fairly and free of bias**, favouritism, personal friendships or self-interest and should not unfairly exclude certain individuals or groups of staff.



# DISCRETIONARY PAYMENTS

## Employers need to understand the difference between different types of discretionary payment and how they should be treated from a legal, taxation and ethical perspective

There are three ways in which customers may choose to pay a gratuity:

- Paying a discretionary service charge shown on a bill
- Adding an extra amount over and above the sale to a card transaction
- Leaving an additional sum in cash

All amounts received by staff deriving from such payments are taxable with deductions of tax at source usually being made by the business when the gratuity is a payment of a service charge or part of a card transaction. Whether National Insurance Contributions are paid will depend on how the monies paid are controlled and managed and by whom.

Tips and service charges cannot be used to meet National Minimum or Living Wage obligations.

### Discretionary service charges and tips paid by card

Under both British and European law all proceeds of discretionary service charges (regardless of whether paid in cash or as a part of a card transaction) are the legal property of the business, as well as any other tips or gratuities paid as a part of a card transaction.

Despite the legal status of such gratuities however, businesses must pass these monies to their staff in full, in line with what the Government believes to be the wishes of consumers. Typically, this is dealt with through a well-managed tronc system which allows for team members from different departments who have contributed to the guest experience to benefit.

### Cash tips

Where a customer pays a tip in cash in lieu of, or in addition to, a discretionary service charge then this is not the legal property of the business.

Your staff may keep their own cash tips, or they may have an informal arrangement to share them out between themselves at the end of the session or night. It is then an employee's personal responsibility to declare this income to HM Revenue & Customs ("HMRC"). Businesses should remind staff (at least annually) of this obligation.

Businesses should refrain from requiring staff to hand over cash tips unless:

- There are specific rules in place (such as in casinos) which make it necessary.
- Staff prefer to have tips pooled and dealt with formally.



# THIRD PARTY ADMINISTRATION COSTS

**It is good practice for businesses to pass 100% of the gratuities they receive (net of costs) to their staff, and confirm this to both customers and employees.**

Businesses incur costs when they collect, administer, process and pay the proceeds of gratuities to staff, with or without a tronc system. Costs may include credit card commissions and fees, bank charges, the costs of any external third party attributable to running and managing the tronc system, and costs incurred in processing tronc via payroll (as is required by law). In some cases, these costs are applied before monies are actually received by the business.

Typically, given current rates of fees and charges levied by banks and credit cards, total administration costs amount to approximately 5% of the gross gratuities paid by customers. It is uncommon and unlikely for these costs to exceed this level.

At the time of writing (October 2018) a business is entitled, if it so wishes, to deduct these essential costs from the gross gratuities available to the staff, but should ensure that both staff and customers are advised of this. In October 2018 the Prime Minister announced that legislation would be forthcoming to ensure that "100% of tips are paid to workers", but it is as yet unclear whether this means 100% of what is paid by consumers or 100% of what is received by businesses after costs.





# TRONC SYSTEMS

**A tronc system should seek to reward all team members who contribute to the quality of the service or the product, and to those who help maintain a motivated, organised and well-trained team to deliver both product and service**

A tronc system is an organised arrangement to share out proceeds from service charges and card tips. One of the principle purposes of a tronc system is to ensure that monies derived from card tips or discretionary service charges are treated the same for tax purposes as if they had been tips paid in cash - for example, by being outside of the scope of VAT and National Insurance Contributions. Without a well-run tronc system, businesses can unwittingly create unintentional taxation costs for employees and themselves.

Additionally, a well-managed tronc system represents the most transparent way of dealing with service charges paid by customers. In its 2016 consultation the Government stated (para 65) that they wished to “explore ways to increase the prevalence of well-managed tronc systems”.

It is down to a business to decide whether to use a tronc system, but, if such a system is used it must be controlled by a member of staff or an independent third party – not by the business.

The principles in this guide:

- support the use of well-managed tronc systems as best practice for both businesses and employees and as a basis of transparency for both workers and consumers; and
- allow for troncs to be run independently, whilst providing businesses with enough oversight (but not control) to satisfy themselves that the tronc is being operated in line with all HMRC requirements and other employment-related obligations (such as without discrimination).





Many different staff in a business play a part in the guest experience; some are visible to the customer and some not.

A fair tronc system should seek to reward all the team who contribute to the quality of the service (servers, hosts, receptionists), the quality of the product (chefs, bartenders, kitchen porters), and to those who help maintain a motivated, organised and well-trained team to deliver both product and service.

The taxation treatment of tronc monies can be complex. If matters are not dealt with correctly the business will be held responsible by HMRC for any shortfall. Businesses will, therefore, always wish to ensure that the tronc is operating in a manner which is legally compliant.

Tronc arrangements which work well are operated with the support of staff, without complaint, and within the framework of the principles set out in this guide.

When a tronc system is introduced for the first time there should be discussions with staff to ensure they understand:

- how the system operates;
- the reasons for introducing the tronc; and
- the impact on employees participating in the tronc

The nature of these discussions will vary depending on the size and structure of the business and need not be formal.

In keeping with the principles of transparency, staff should always be aware of the rules of the tronc scheme, information about how their own share is calculated (e.g. points, minimum rates, equal share), the identity of the Troncmaster, and how to raise or ask questions regarding the operation of their scheme.





# THE ROLE OF THE TRONCMASTER

**The Troncmaster is responsible for ensuring that the tronc is run in a way that is fair to all members, without favouritism, bias or discrimination.**

The Troncmaster may be an employee of the business or an independent third party. They may act alone, in conjunction with informal staff representatives, or with a formal committee, depending on the size and structure of the business.

Whilst the Troncmaster is always appointed by the employer, they should act with the consent of the team and their appointment should be ratified annually by their members.

The rules of the tronc system, which include the method or criteria for allocating the funds, should be made available to all staff in writing. Tronc members should be advised of any material changes to these rules.

Each pay period, the Troncmaster should ensure members are provided with enough information to enable them to check:

- the calculation of their own tronc award; and that
- the Troncmaster has applied the rules of the scheme correctly and consistently.

At least once a year, the Troncmaster should make a simplified account of the tronc system available to all members. The account should show:

- total funds for distribution made available to the Troncmaster by the business;
- funds distributed to members; and
- any undistributed funds held in reserve.

Details of all tronc allocations and distributions will be made available to the business. This is so the business can check that the Troncmaster is acting:

- in accordance with the rules of the tronc;
- in line with all relevant regulations and legislation; and
- fairly and transparently, without impropriety or abuse of position.

All members should have access to the Troncmaster either in person, by telephone or by email. The Troncmaster should deal with and respond to any reasonable requests and queries raised by members.

## Resolving disputes

Where a member of a tronc system disagrees or objects to a decision taken by the Troncmaster they should initially raise the matter with the Troncmaster themselves. Troncmasters should commit to taking such objections seriously and investigating them fully and impartially.

Where a member is unsatisfied with any findings from the Troncmaster - or feels unable to raise the matter with the Troncmaster in person due to the nature of the complaint or the conduct of the Troncmaster - then the Troncmaster should agree to a review being undertaken by a suitable independent third party. This third party could be a professional, legal or HR advisor or an organisation such as ACAS.

## Annual ratification

Although appointed by the business, it is best practice for the Troncmaster to seek a ratification from the members of the tronc. They should do this at least annually to satisfy themselves and the business that they retain the members' confidence.

The process used to ratify the Troncmaster will vary from business to business but should ensure that the view of each department is fairly represented in the vote. Should the outcome be a vote of 'no confidence' in the Troncmaster, the business should move to appoint a new Troncmaster.

# CUSTOMER COMMUNICATIONS

**Customers should be made aware of the existence of a service charge, and its discretionary nature, before placing an order.**

Typically, this is by way of a statement on the menu. The statement should be clear and unambiguous.

Customers should never feel pressured into paying a service charge and any requests to remove the charge should not be challenged.

In addition, customers should be clearly advised if a tronc system exists, who manages it (for example, a member of staff or an independent third party), and which groups of staff benefit.

A detailed menu statement might read as follows:

*"A discretionary service charge of 12.5% will be added to your bill, all of which is shared among all of our team (including servers, bartenders, chefs, kitchen porters, receptionists and supervisors) through an independently-managed tronc system. Further details are on our website. Please tell your server if you do not wish to pay the discretionary service charge."*

A business should provide additional details on their website, particularly if an edited statement only is shown on the menu due to space limitations. A copy of the rules of the tronc should be freely available to customers on request.







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