No. 01-463

IN THE

Supreme Court of the United States

UNITED STATES OF AMERICA,

Petitioner,

v.

FIOR D'ITALIA, INC.

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF AMICUS CURIAE FOR THE AMERICAN GAMING ASSOCIATION IN SUPPORT OF RESPONDENT

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BRIEF AMICUS CURIAE FOR THE AMERICAN GAMING ASSOCIATION IN SUPPORT OF RESPONDENT

STATEMENT OF INTEREST OF AMICUS CURIAE

The American Gaming Association ("AGA") is a nonprofit trade association that represents the commercial casino industry in addressing federal legislative and regulatory issues.[1] It also serves as a clearinghouse for information,

[1] Pursuant to this Court's Rule 37.6, we note that no part of this brief was authored by counsel for any party, and no person or entity other than the American Gaming Association or its members

develops educational and advocacy programs, and provides industry leadership in addressing issues of public concern. AGA has 19 casino members who own or operate 151 gaming properties, accounting for approximately three-quarters of commercial gaming revenue in the country. AGA members employ a broad range of workers who receive tips from customers in the course of their employment, including food and beverage workers, casino gaming staff, hotel bell staff, and parking valets.

In this case, the Ninth Circuit ruled that the Internal Revenue Service ("IRS") may not determine an employer's share of Federal Insurance Contribution Act ("FICA") taxes under 26 U.S.C. § 3111 on the basis of an aggregate estimate of the tips received by the employer's tipped workforce as a whole. Rather, the Ninth Circuit held, the IRS must determine the employer's share of FICA taxes on an employee-by-employee basis using the actual tips received by each employee. In light of the number of tipped workers in their employ, AGA members have a direct and substantial interest in this question. AGA members also have substantial historical experience with the evolution of the Federal tax laws governing an employer's FICA tax obligation with respect to tipped employees.

This brief is filed with the written consent of all parties pursuant to this Court's Rule 37.2(a). Copies of the requisite consent letters have been filed with the Clerk.

STATEMENT OF THE CASE

Employers such as hotels, restaurants, and casinos typically employ various workers—including waiters, bell staff, and parking valets—who derive part of their earnings from tips received from customers. Some of these employees, such as table bussers, bartenders, and floor captains, receive tips

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made any monetary contribution to the preparation or submission of the brief.

indirectly from other workers who share their tips with them. All tips earned by employees are "deemed to have been paid by [their] employer[s]," who must pay FICA taxes on those tips deemed "wages" for FICA tax purposes. 26 U.S.C. §§ 3111, 3121(q).[2]

Employers, however, face both practical and legal obstacles that severely limit their ability to determine the amount of tips earned by their tipped employees. To begin with, an employer has little control over whether and how much an employee may be tipped for a particular service. Tips are generally bestowed at the customer's discretion, in an amount determined by the customer. The employer is not a party to the tip transaction. An employee's tips may vary greatly depending on the time of day, day of week, service area location, level of staffing, occupancy rate of a facility, the employee's personality and efficiency, method of payment (cash or credit card), and the employee's generosity in sharing tips with co-workers. According to a study by the IRS of tipping practices in the food service industry, "[c]ustomers failed to leave tips on close to nine percent of the gross receipts of the establishments." U.S. Department of the Treasury, Internal Revenue Service, Research Division, *Tip Income Study: A Study of Tipping Practices in the Food Service Industry for 1984*, Publication 1530 (August 1990) (Catalogue Number 12482K), at 4.

Industry experience, moreover, is that a high percentage of tips are made in cash. According to the IRS study, "[c]harged tips were left on only 20 percent of the total

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[2] "Wages" for FICA tax purposes include all tips except those received by an employee who earns more than $20 in tips any given month, and those which exceed the Social Security wage base. 26 U.S.C. §§ 3121(a)(1), (a)(12)(B), 3121(q). Those amounts establish what is known as the "wages band." *See* Pet. App. 3a-4a. Only those tips falling within the wages band are subject to FICA taxes.

amount of the establishments' gross receipts, while cash tips were left on over 71 percent of total receipts." *Id*. Indeed, some employees—such as parking valets and bell staff—receive only cash tips. Receipts from cash transactions reflect only the charge for items such as food and beverages, not any gratuity left by the customer for an employee. Because cash tips are paid by customers directly to employees, an employer has no way of knowing the amount of cash tips an employee has received.

Nor can the employer accurately determine what an employee earns in tips from credit card receipts. Although credit card receipts may indicate the amount of a tip received by an employee from a customer, such receipts will not reflect tips passed along by the employee to co-workers such as bus or bar staff. Any effort to use credit card receipts as the basis for reporting employee tips would impose an onerous administrative burden on the employer. Employers in the gaming industry, for instance, would be faced with the difficulty and heavy expense of trying to integrate three different computer systems, in order to transfer data from the point-of-sale system to the time and attendance system, and then to the payroll system.

In addition to such practical difficulties, employers may face legal obstacles to determining the amount of tips earned by employees. State labor laws sharply restrict any potential employer involvement with tips. *See, e.g.*, Cal. Labor Code § 351; Nev. Rev. Stat. § 608.10. In California, for example, an employer may not "collect, take, or receive any gratuity or part thereof that is paid, given to, or left for an employee by a patron." Cal. Labor Code § 351. The law declares that "[e]very gratuity is * * * to be the sole property of the employee or employees to whom it was paid, given, or left for." *Id.* Similarly, in Nevada, it is unlawful for any person to "[t]ake all or part of any tips or gratuities bestowed upon his employees." Nev. Rev. Stat. § 608.10. Such laws effectively prevent employers from exercising any significant

control over an employee's tips. As a result, employers have simply no way of ascertaining the actual tip income of their employees.

The amount of tips earned by an employee is thus uniquely within the employee's knowledge and control. Not surprisingly, when it comes to tip income, the core mechanism of the FICA tax system adopted by Congress reflects this reality by focusing on the reporting of tips by the employee to the employer, upon which the employer may rely. The Social Security Amendments of 1965, Pub. L. No. 89-97, 79 Stat. 286 (1965), extended Social Security and FICA coverage to tips for the first time. As a committee report on that legislation noted:

> The principal difficulty [in extending social security coverage to tips] has been to devise a fair and practical system for obtaining information on amounts of tips received by an individual which could serve as a basis for contributions and benefit credits. * * * The committee has * * * decided that the only equitable way of counting tips toward benefits is on the basis of actual amounts of tips received and that *the only practical way to get this information is to require employees to report their tips to the employer*. [H.R. Rep. No. 89-213, at 96 (1965) (emphasis added).]

Accordingly, all tipped employees must submit monthly reports to their employers of all tips received that constitute "wages." 26 U.S.C. § 6053(a).[3] Congress placed the onus of compliance with this employee-based reporting system squarely on the employee by subjecting any employee who fails to report all tips to a penalty in an amount equal to 50 percent of the employee's share of FICA tax on such unre-

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[3] The tip report may be made on Form 4070 or in another written statement. 26 C.F.R. § 31.6053-1(b)(2).

ported tips (in addition to the employee's share of FICA tax otherwise due). *See id*. at § 6652(b).

Using the tip report provided by the employee, the employer withholds from the employee's wages the employee's share of FICA tax on reported tips. *See* 26 U.S.C. § 3102(c)(1). The employer also uses the employee's tip report to determine its own share of FICA taxes. To calculate that share, the employer uses Form 941 ("Employer's Quarterly Federal Tax Return"), which combines the employer and employee FICA tax rates into a single overall rate. That rate is applied to all "taxable social security tips"—defined by the IRS for this purpose as "all tips *your employees reported* during the quarter," up to the Social Security wage base. Internal Revenue Service, "Instructions for Form 941 – Employer's Quarterly Federal Tax Return," at 3 (Rev. January 2002) (emphasis added).[4] The employer also reports "such tips as are included in statements furnished [by the employee] to the employer" to the IRS and the employee on Form W-2 as taxable wages of the employee for the year. 26 U.S.C. § 6051(a).

SUMMARY OF ARGUMENT

In this case, the IRS seeks to improperly shift its responsibility for policing employee tip compliance to the employer. As the language and legislative history of congressional enactments regarding FICA taxes over the last several decades make clear, Congress has steadfastly refused to impose this burden on employers.

Tips are uniquely within the knowledge and control of the employee. The employer lacks the ability, independent of reports from employees, to determine, verify, or exercise control over the tips received by an employee. The tip

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[4] IRS forms and instructions are contained in IRS Pub. 1132, *Reproducible Copies of Federal Tax Forms and Instructions* (2000).

transaction occurs solely between the customer and the individual employee; the employer is not a party to the transaction. Because of the employee's knowledge and control over the tips and the employer's lack of such knowledge and control, the core mechanism of the FICA tax system adopted by Congress is the reporting of tips by the employee to the employer, upon which the employer may rely.

The focus of Congress in adopting the statutory regime governing tip compliance for FICA tax purposes has been on encouraging the employee to make the proper tip report to the employer and on providing the IRS with the tools to audit the individual employee on his or her income, tip reports, and books and records. This is a responsibility that the IRS now disclaims in the case at hand. Rather, the IRS would require the employer to make an entirely different computation of tips for purposes of the employer's share of the FICA tax—as simply an aggregate estimate for the employer's workforce as a whole based upon an assumed flat percentage of the employer's gross sales. Under the IRS's approach, the individual employees are not reviewed, and no attempt is made to correlate this artificial construct of an aggregate estimate of tips for the employer's workforce as a whole with the actual tip income of any particular employee.

The result of the IRS's FICA tax assessment solely against the employer using an aggregate estimate is to place the burden on the employer to somehow independently quantify the amount of tip payments the employee has received from customers. The IRS seeks to force the employer to prove the negative—that its employees did not receive tips over and above those reported to the employer—in tipping transactions to which the employer was never a party and had no direct knowledge of the particular circumstances. Such IRS efforts to shift the burden of responsibility to the employer for tip determination, auditing, and enforcement have been consistently rejected by Congress.

Accordingly, an IRS assessment of FICA tax on the employer based solely upon an employer-only audit using the artificial construct of an aggregate estimate of tips for the employer's workforce as a whole based upon an assumed flat percentage of the employer's total gross sales—without regard to the actual tips of any employee—is unauthorized and invalid. Prior to approaching the employer, the IRS first must discharge its responsibility to conduct audits of the individual employees to determine whether an employee has underreported actual tip income.

ARGUMENT

I. NOTHING IN THE INTERNAL REVENUE CODE AUTHORIZES THE IRS TO USE AN AGGREGATE ESTIMATE OF TIPS TO ASSESS AN EMPLOYER'S SHARE OF FICA TAXES.

1. As discussed, the actual amount of tips earned by an employee is uniquely within the employee's knowledge and control, and employers lack the ability to determine how much an employee has earned in tips. Thus, as the Ninth Circuit correctly concluded below, if the IRS believes that members of an employer's workforce have underreported tips, "there is no way to determine [an] employer's tax liability without making an employee-by-employee determination of the taxable tips each has earned." Pet. App. 13a.

In this case, the IRS did not make such individual determinations in assessing the employer's liability. Instead, the agency chose to make an aggregate estimate of tips earned by the employer's workforce as a whole based on an assumed flat percentage of the employer's total gross sales. Nothing in the Internal Revenue Code authorizes the IRS to use such a method to determine an employer's share of FICA taxes.

In the courts below, the Government relied heavily on Section 3121(q) of the Internal Revenue Code as a basis for its purported authority to use an aggregate estimate of tips to assess an employer's FICA liability. *See* Pet. App. 10a-11a,

41a-42a. That section provides that tips received by an employee are "deemed to have been paid by the employer" for FICA tax purposes. 26 U.S.C. § 3121(q). It further provides:

> Such remuneration shall be deemed to be paid at the time a written statement including such tips is furnished to the employer pursuant to section 6053(a) or (if no statement including such tips is so furnished) at the time received; except that, in determining the employer's liability in connection with [its share of FICA taxes] with respect to such tips in any case where no statement including such tips was so furnished (or to the extent the statement so furnished was inaccurate or incomplete), such remuneration shall be deemed for purposes of subtitle F to be paid on the date on which notice and demand for such taxes is made to the employer by the Secretary. [*Id*.]

The Government maintains that because Section 3121(q) "provides 'that an employer can be assessed for its share of FICA taxes on employee tips even if the employee fails to report all tips,' " it "thereby 'suggests that the employer can be assessed its share of FICA taxes even when the individual employee's share is not determined.' " Pet. Br. 16 (quoting *Morrison Restaurants, Inc.* v. *United States*, 118 F.3d 1526, 1529 (11th Cir. 1997)).

Nothing in Section 3121(q), however, suggests that an employer may be assessed its share of FICA taxes when the amount of tips actually earned by the individual employee has not been determined. The statute merely provides that where an employee fails to provide a statement of tips to an employer or where the statement provided is inaccurate or incomplete, such tips "shall be deemed for purposes of subtitle F to be paid on the date on which notice and demand for such taxes is made to the employer." 26 U.S.C. § 3121(q). The purpose of this language is to clarify timing issues, not to confer substantive powers upon the IRS.

Subtitle F contains the procedural and administrative provisions of the Internal Revenue Code, including those concerning the limitations period for assessments and collection (Section 6501), and the accrual of interest on unpaid taxes (Section 6601). Thus, all Section 3121(q) does is establish limitations and interest accrual periods in cases where an employee has failed to report all tips.

It is of no help to the Government that Section 3121(q) contemplates that an employer may be liable for its portion of FICA taxes even where an employee fails to report all tips. As the Ninth Circuit below observed, "[n]othing in the text of section 3121(q) speaks to the *method* the IRS may use in making its assessment." Pet. App. 11a (emphasis in original). Indeed, the most sensible reading of the statute is that Congress wanted to ensure that the IRS would have the opportunity to assess an employer its share of FICA taxes in the event it audited an employee and discovered unreported tips. If the normal limitations period applied, that opportunity might be lost. As the Ninth Circuit explained, "Section 3121(q) solves this problem by keeping the period open indefinitely—which means for however long it takes to complete [an] audit of the [taxpayer's] tipped employees." Pet. App. 12a.[5]

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[5] The Government seeks support for its interpretation in a statement in the Conference Report to the legislation that enacted the current version of Section 3121(q) to the effect that the employer portion of the FICA tax must be paid " 'on the total amount of wages and cash tips up to the Social Security wage base.' " Pet. Br. 16 (quoting H.R. Conf. Rep. No. 100-495, at 802 (1987)). But that statement no more answers the question whether the IRS may use an aggregate estimate of tips than the statute itself. Rather, the statement merely describes a change in the law rendered by the enactment of the current version of Section 3121(q). Prior to that enactment, an employer's share of FICA taxes on tip income was limited to tips counted towards the federal minimum wage. *See* Pet. Br. 16 n.12. The current version of Section 3121(q) extends the employer's FICA tax obligation to all

2. The Government now asserts that the "correct[] * * * source of the agency's general authority to use estimates in making FICA tax assessments" is Section 6201 of the Internal Revenue Code. Pet. Br. 23. That section simply authorizes the Secretary of the Treasury to "make the inquiries, determinations, and assessments of all taxes * * * imposed by this title." 26 U.S.C. § 6201(a). It by no means grants the IRS the authority to use any particular method of assessment, much less the method employed by the IRS here. Nevertheless, the Government maintains that Section 6201 " 'implicitly authorizes the IRS to use an indirect formula.' " Pet. Br. 24 (quoting *Bubble Room, Inc*. v. *United States*, 159 F.3d 553, 565 (Fed. Cir. 1998)). But as Judge Plager noted in his dissent in *Bubble Room*, "[t]hat is akin to saying that a statute that authorizes the [IRS] to adopt rules and regulations implicitly authorizes whatever regulations the [IRS] adopts, regardless of their scope or content." 159 F.3d at 571. The Government's contention that "there is " 'no other way to 'determine and assess' the wages deemed to have been paid by the employer' " is simply wrong. Pet. Br. 24 (quoting *Bubble Room*, 159 F.3d at 565). As we have explained, there is another, and much better, way to determine an employer's FICA liability—"by making an employee-by-employee determination of the taxable tips each has earned." Pet. App. 13a.[6]

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tips falling within the wages band. The statement in the Conference Report simply makes that clear.

[6] The Government argues that "[b]ecause an employer is not assessed the employer FICA tax separately for each employee, there is no requirement that the tax be calculated based upon individual employee determinations." Pet. Br. 20. As support for that proposition, the Government notes that "[a]s shown on [Form 941], employer FICA taxes are imposed on the aggregate amount of tips and other wages received by *all* of the employer's employees." *Id*. (emphasis in original). What the Government overlooks, however, is that the IRS's instructions to Form 941 only require

3. The Government also relies on Section 446(b) of the Internal Revenue Code as support for its purported authority to make the assessment at issue here. *See* Pet. Br. 20-23. That section provides that "[i]f no method of accounting has been regularly used by the taxpayer, or if the method used does not clearly reflect income, the computation of taxable income shall be made under such method as, in the opinion of the Secretary, does clearly reflect income." 26 U.S.C. § 446(b). Section 446(b) thus gives the IRS the authority to use estimates to determine the amount of an employee's unreported tips for income tax purposes. *See, e.g.*, *McQuatters* v. *Commisioner*, 32 T.C.M. (CCH) 1122 (1973).

As the Ninth Circuit held below, "the IRS cannot rely on section 446 as authority for the assessment here because the section does not apply to the collection of *FICA* taxes." Pet. App. 10a (emphasis added). By its terms, Section 446(b) applies only to the computation of *income* taxes. The Government recognizes as much, but suggests that Section 446(b) should somehow be "informative." Pet. Br. 22. Employers are in such a different position from their employees with respect to tips, however, that Section 446(b) simply has no relevance here.

Tipped employees, like everyone else, are required to report their income to the IRS and to maintain adequate records of income—including, in their case, tips. *See, e.g.*, *Anson* v. *Commissioner*, 328 F.2d 703, 705 (10th Cir. 1963) ("[T]he privilege of original self-assessment accorded the taxpayer carries with it the burden of support through maintenance of records which clearly and accurately reflect income.") If an employee fails to discharge its reporting and recordkeeping duties, Section 446 specifically authorizes the IRS to undertake a reasonable reconstruction of the employee's income.

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the employer to calculate its share of FICA taxes on *reported* tips. *See supra* at 6.

See 26 U.S.C. § 446(b).[7] Because the employee actually receives the tip income, the employee is uniquely in a position to challenge an assessment based on an estimate of the tips the employee has earned. *See, e.g., Anson*, 328 F.2d at 705 ("The cumulative amount of gratuities received is peculiarly within the knowledge of the recipient and is not subject to exact verification from records kept by the employer, the contributor, or others.").

The employer, by contrast, is not required to keep records of tip income, except to the extent the employee reports tips to the employer under the employee-based tip reporting system adopted by Congress. Apart from what has been reported by the employee, the employer has no idea how much the employee has earned in tips. *See, e.g.*, Pet. App. 7a ("While each employee knows how much he receives in tips, the restaurant does not."). Thus, unlike an employee who actually receives tips, an employer is not in any position to challenge an estimate of its FICA tax liability. Unlike the IRS, the employer cannot audit its employees to establish the actual amount of their tip income.

As the Ninth Circuit recognized, "[f]orcing [the employer] to prove that [an] estimate is wrong puts an impossible burden on it." Pet. App. 8a. This is especially troubling where, as here, the employer has discharged its reporting and recordkeeping duties and thus done everything required of it by law. *See id.* ("Unlike the taxpayers in *McQuatters* and

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[7] In *McQuatters*, for instance, the taxpayers were unable to produce records of their actual tip income or demonstrate that they had done a significant amount of "low tipping" work. *See* 32 T.C.M. (CCH) at __. Thus, it was deemed entirely appropriate for the IRS to use an estimate to determine their unreported tip income. *Id*. at 1125. *See also Mendelson* v. *Commissioner*, 305 F.2d 519, 523 (7th Cir. 1962) (upholding assessment based on estimate of tip income where taxpayer failed to keep records of such income).

Mendelson, then, the taxpayer in [this] case did not fail to satisfy a legal duty imposed on it by the Internal Revenue Code, and thus did not give the IRS just cause for resorting to an estimate in constructing its assessment.").[8] For such reasons, no doubt, Congress has not authorized the IRS to use such estimates in FICA tax cases as it has in income tax cases.[9] If the IRS believes that an employer is liable for additional FICA taxes because employees have underreported tips, the IRS must proceed in the only manner permitted by law—by making individual determinations of actual tip income.[10]

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[8] The cases cited by the Government involving the use of estimates to reconstruct a taxpayer's unreported income are therefore wholly inapposite. *See* Pet. Br. 21-22.

[9] The Government seeks to have it both ways in quibbling over whether Section 446(b) in fact specifically authorizes the IRS to use estimates in income tax cases. *See* Pet. Br. 22-23. In providing that the IRS may compute taxable income "under such method as, in the opinion of the Secretary, does clearly reflect income," 26 U.S.C. § 446(b), Congress plainly gave the IRS "broad authority to use estimates in making income tax assessments." Pet. App. 10a. The absence of a similar provision giving the IRS such authority in FICA tax cases is a strong indication in and of itself that Congress did not intend the IRS to have such authority. *See Barnhart* v. *Sigmon Coal Co.*, 122 S. Ct. 941, 951 (2002) ("[I]t is a general principle of statutory construction that when 'Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion' ") (quoting *Russello* v. *United States*, 464 U.S. 16, 23 (1983)).

[10] Contrary to the Government's assertion, an aggregate estimate of tips earned by the employer's workforce as a whole based on an assumed flat percentage of the employer's gross sales is *not* "far more likely to achieve factual accuracy" than individual determinations of tip income. Pet. Br. 25. As we have explained, because the amount of tips actually earned is peculiarly within the

II. CONGRESS HAS STEADFASTLY REFUSED TO ALLOW THE IRS TO SHIFT THE BURDEN OF ENFORCEMENT TO EMPLOYERS.

The result of an assessment based on an aggregate estimate of tips is to put on the employer the burden of independently quantifying the amount of tips an employee has received from third-party customers. Accordingly, the assessment method used in this case effectively shifts from the IRS to employers the agency's responsibility to ensure compliance with the Code's tip reporting requirements.

Such an approach plainly contravenes congressional intent. In a series of enactments over the last 30 years, Congress has consistently blocked efforts by the IRS to shift the burden of tip reporting enforcement to employers—who, after all, are distinctly ill-equipped to police the tip reporting of their employees. Congress's steadfast refusal to allow the IRS to shift its responsibility to employers precludes an interpretation of the Code that authorizes the assessment method used here. *See, e.g.*, *FDA* v. *Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 155-156 (2000) (legislative enactments over the years precluded an interpretation of the Food, Drug, and Cosmetic Act which gave the FDA jurisdiction to regulate tobacco products).[11]

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knowledge of employees, they are uniquely positioned to challenge an estimate of the tips they have earned. As a result, individual determinations of tip income are in fact more likely to be accurate, and will not necessarily yield the same result as the aggregate estimate method the Government advocates here. Indeed, such individual determinations are the only way to segregate tips falling within the "wages band" from aggregate tips, since those amounts cannot be determined unless an individual employee's tip income is known.

[11] As this Court has held, "the implications of a statute may be altered by the implications of a later statute." *United States* v. *Fausto*, 484 U.S. 439, 453 (1988). All the legislation discussed

In 1976, Congress invalidated a pair of IRS rulings which would have made employers responsible for determining a portion of their employees' tip income. Those rulings required employers to report on Form W-2 all tips included on credit card receipts and paid over in cash to an employee by the employer, regardless of whether the employee reported such tips to the employer. *See* Rev. Rul. 75-400, 1975-2 C.B. 464 (1975); Rev. Rul. 76-231, 1976-1 C.B. 378 (1976). Congress moved quickly to squelch that requirement by retroactively suspending the effect of the IRS's rulings. *See* Pub. L. No. 94-455, § 2111, 90 Stat. 1520, 1905 (1976) ("Tax Reform Act of 1976"); S. Conf. Rep. No. 94-1236, at 498 (1976).

In the Revenue Act of 1978, Congress made that prohibition against employer charge tip reporting permanent by adopting what is now Section 6041(e) of the Code. *See* Pub. L. No. 95-600, § 501(b), 92 Stat. 2763, 2878 (1978); 26 U.S.C. § 6041(e).[12] The Conference Report accompanying the bill containing Section 6041(e) emphasized that "the only employee tips which an employer must report to the IRS are those reported to the employer by employees." H.R. Conf. Rep. No. 95-1800, at 271 (1978). The Senate Committee Report further explained that "an employer will be required to keep charge receipts (which receipts reflect the amount of

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below was passed after the enactment in 1954 of Section 6201(a), *see* Pub. L. No. 83-591, § __, 68A Stat. 3, 767 (1954) ("Internal Revenue Code of 1954"), the general provision which the Government claims "broadly authorizes" the IRS to use an aggregate assessment method. Pet. Br. 23. *See also Busie* v. *United States*, 446 U.S. 398, 406 (1980) ("a more specific statute will be given precedence over a more general one, regardless of their temporal sequence").

[12] Section 6041(e) exempts tips required to be reported by employees to employers under Section 6053(a) from Section 6041(a) (requiring employers to report to the IRS total earnings paid to an employee), on which the IRS's rulings were based.

tips included by the customer in the charged amount), but may not be required to record on such charge receipts, or otherwise keep records of (except copies of [employee] sec. 6053(a) statements), the name of any particular employee to whom the charge tip amount is paid over by the employer." S. Rep. No. 95-1263, at 213 (1978). As the Senate Committee explained in rejecting the IRS's attempt to impose such requirements upon employers:

> [R]equiring employers to report to the IRS charge account tips paid to employees on the basis of charge receipts (as sought to be imposed by Revenue Rulings 75-400 and 76-231) would place *unnecessary recordkeeping and reporting burdens on the employer* and would fail to provide the IRS with precise information on the amount of tip income taxable to particular employees. [*Id.* at 212 (emphasis added).]

In its most recent comprehensive review of the tip compliance rules for FICA tax purposes, Congress continued its longstanding focus on *employee* compliance by adopting a provision to improve tip reporting by the employee to the employer. In the "Tax Equity and Fiscal Responsibility Act of 1982," Congress enacted a requirement that food and beverage establishments with ten or more employees report certain information to the IRS, including the employer's gross receipts, the aggregate amount of charge receipts, and the aggregate amount of charge tips. *See* Pub. L. No. 97-248, § 314(a) (1982); 26 U.S.C. § 6053(c)(1). Congress also required that, if an employer's tipped employees as a whole have reported tips totaling less than 8 percent of the employee's gross receipts, the employer allocate the shortfall among its tipped employees. *See id*. at § 6053(c)(3). Each employee's allocated tips are reported to the IRS and to the employee. *See id*. at § 6053(c)(1)(E), (2)(C).

As the Conference Report to the legislation makes clear, the purpose of these new recordkeeping and reporting

requirements was to provide the IRS with additional information to assist the agency in *its* enforcement efforts:

> [T]he rules of present law relating to reporting of tips to employers by their employees and to the resulting withholding of FICA and income taxes is retained. However, *to assist the Internal Revenue Service in its examinations of returns filed by tipped employees*, the bill provides a new set of information reporting requirements for large food and beverage establishments and, under certain circumstances, a tip allocation requirement. [S. Conf. Rep. No. 97-530, at 556-557 (1982) (emphasis added).]

The Conference Report also makes clear that Congress believed that the new requirements would ensure more accurate tip reporting by employees:

> The 8-percent figure reflects the conferees' judgment that the tip rate in establishments subject to this reporting requirement will rarely be below the 8-percent level. *Thus, an employee who reports less than his allocated amount of tips must be able to substantiate his reporting position with adequate books and records (as he must under present law)*. * * * Employees would be put on notice that their returns would be identified for audit unless this 8 percent tip reporting is satisfied. [*Id*. at 557-558 (emphasis added).]

Congress specifically refrained from requiring employers to make any determination of tip income based on the information they are required to report. *See id*. at 557 ("The allocation of this 8-percent amount to employees for reporting purposes will have no effect on the FICA or income tax withholding responsibilities of the employer or on his FUTA obligations. Thus, employers will continue to withhold only on amounts reported to them by their tipped employees."). As the Senate Committee report makes clear, that responsibility was to remain with the IRS:

> Expanded information reporting on tip income will encourage better reporting of such income by its recipients and facilitate Internal Revenue Service efforts to increase compliance in this area. At the same time, the committee recognizes that improved compliance rules should not impose unnecessary recordkeeping obligations on taxpayers or employers. [S. Rep. No. 97-494, at 251-252 (1982).]

In recent legislation, Congress demonstrated once again its refusal to impose the burden of enforcement on the employer. Responding to industry complaints of IRS heavy-handedness, Congress took the extraordinary step of enacting a law directing "[t]he Secretary of the Treasury [to] instruct employees of the Internal Revenue Service that they may not threaten to audit any taxpayer in an attempt to coerce the taxpayer into entering into a Tip Reporting Alternative Commitment [("TRAC")] Agreement." *See* Pub. L. No. 105-206, § 3414, 112 Stat. 755 (1988) ("Internal Revenue Service Restructuring and Reform Act of 1998."). Under a TRAC agreement, an employer agrees to establish new tip reporting procedures, educate its employees about their tip reporting responsibilities, and fulfill various other requirements. In return, the IRS agrees to base the employer's FICA tax liability solely on reported tips and unreported tips discovered in individual audits of employees. *See* Pet. Br. 30.[13] Congress thus made clear that employers cannot be made to undertake the burden of ensuring tip reporting compliance among their employees.[14]

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[13] The IRS has declined to permit the casino industry to participate in the TRAC program.

[14] The Government contends that this enactment "reflects the understanding of Congress that, in the absence of a TRAC agreement, the IRS has full authority to make aggregate assessments against employers without making determinations with respect to individual employees." Pet. Br. 30. That inference does not hold

These actions by Congress clearly manifest a policy against saddling employers with the responsibility of ensuring accurate tip reporting by their employees. Indeed, as in *Brown & Williamson*, *supra*, "this is not a case of simple inaction by Congress that purportedly represents its acquiescence in [a particular] position," 529 U.S. at 155, but one in which Congress has affirmatively and unequivocally expressed its intent. Against this backdrop, an inference that the Code implicitly authorizes the IRS to use an assessment method that shifts the burden of enforcement to employers is untenable.

As one court rejecting the use of an aggregate estimate has put it, "The United States would have [the employer] be its watchdog [but] that it is not contemplated [by the Code]. * * * If the United States is concerned with dishonest taxpayers it has the means to investigate them; but the investigative burden should not be shifted to the withholding employer in the absence of Congressional intent to do so." *Norfolk Yacht and Country Club* v. *United States*, 1975 WL 731, at *7 (E.D. Va. 1975).

* * *

In sum, Congress has made quite clear over the last several decades that the IRS may not shift to employers its responsibility to ensure tip reporting compliance. The entire focus of Congress in adopting the statutory regime governing tip compliance has been on encouraging the employee to make the proper tip report to the employer and on providing the IRS with the tools to audit the individual employee on his or her income, tip reports, and books and records—a responsibility the IRS now disclaims in the case at hand. An assessment by the IRS of FICA tax on the employer based solely upon an employer-only audit using the artificial construct of

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up against Congress's repeated refusal to allow the IRS to shift its enforcement responsibilities to employers,.

an aggregate estimate of tips for the employer's workforce as a whole—without regard to the actual tips of any employee—is unauthorized and invalid. Prior to approaching the employer, the IRS first must discharge its responsibility to conduct audits of the individual employees to determine whether an employee has underreported actual tip income.

CONCLUSION

For the foregoing reasons, the judgment below should be affirmed.

Respectfully submitted,

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