

Example 1: Olga is single with no dependents. She has a valid Social Security number. Olga works as a server. Her income is from one restaurant and is reported on a W-2; she did not have any unreported tips to report on Form 4137. Her total income for the year was \$32,000, and \$19,000 is reported in Box 7 of her W-2 as Social Security Tips. Using the interview tips, you should be able to determine that Olga qualifies for the tip deduction, but it is limited to the \$19,000 of tips she actually received.

Example 2: Pablo is single and has a valid Social Security number. Pablo is a part-time rideshare driver. As a self-employed taxpayer, his income, including tips, is reported on a Form 1099-K. His rideshare income totals \$19,000, including \$11,000 in tips. After deducting Pablo's mileage, tolls, and other necessary and ordinary business expenses, Pablo's Schedule C shows a net profit of \$5,000, which includes his tips as income. Pablo also works as a computer technician for a local electronics store. In this job, he earned \$42,000, which was reported on form W-2. He did not receive any tips at this job. Pablo's income is well below the threshold amount of \$150,000. But although he received tips of \$11,000, he earned those tips through his self-employment. His tip deduction cannot exceed the net profit of the trade or business from which he earned the tips. Because his net income on this Schedule C was \$5,000, his tip deduction is limited to \$5,000. And remember that Pablo will still have to pay the self-employment tax on that \$5,000.

Example 3: Quantella is a self-employed hairstylist. Her gross receipts on Schedule C total \$50,000, and \$10,000 of that amount came from tips. Her expenses were \$15,000. Quantella only accepts cash or check payments, so there is no tax form reporting the income. (If Quantella was paid by credit card, Venmo or something similar, the payment processor might issue a tax form that could potentially split the income for her.) The math on this would be simple enough: \$50,000 gross receipts - \$15,000 expenses = a net profit including tips of \$35,000. Since Quantella's tips total \$10,000, and her Schedule C profit exceeds this amount, she has \$10,000 in tips that could be qualified. However, the tip income must be reported on tax forms such as a Form W-2, Form 1099-NEC, Form 1099-K, or Form 1099-MISC.

Since no reporting document exists, the tips do not meet the conditions to be qualified and the deduction is not allowed.

