



Insight

Changes to Tip Regulations

ISABEL SOTO | OCTOBER 17, 2019

Executive Summary

On October 8, The Department of Labor [proposed a rule](#) that would allow for changes to tip regulations under the Fair Labor Standards Act. The most recent changes are an attempt to simplify and clarify the rules around tip credits and to expand which employees can receive tips. The rule could have the following effects:

- The proposed rule would clarify when an employer can claim a tip credit and make additional earnings available to non-tipped workers through more inclusive tip sharing;
- Back-of-house workers could see their wages rise as a result of being included in tip pools, which this rule would allow for the first time; and
- Traditionally tipped workers could potentially see their wages drop slightly, as employers could reduce the overall time tipped workers spend on tip-generating work and could allow non-tipped workers to benefit from tip-pooling arrangements.

Background

Waiters, movers, drivers, and many others employed by the service industry regularly receive tips as part of their work. Some employees can regularly make more in tips than hourly wages while others receive tips as a small supplement to their hourly wages. Due to the variation in tip structure and employee reliance on tips, regulation around tipped work has been complex and sometimes inconsistent. The Department of Labor (DOL) has proposed a rule that seeks to simplify these regulations and expand eligibility for tips.

The current federal minimum wage, set by the Fair Labor Standards Act (FLSA), requires employers to pay their employees \$7.25 an hour. In businesses where employees regularly receive tips—to be considered a “[tipped employee](#)” the worker must make at least \$30 in tips a month—employers may elect to meet their minimum wage requirement by paying less than \$7.25 in hourly wage as long as the tips the employee receives brings total earnings up to \$7.25 an hour. (Certain states will have different requirements due the differences between state and federal minimum wage levels .)

The portion of the employee’s earnings covered by tips and not an hourly wage can be claimed as a “tip credit” by the employer. The maximum tip credit amount an employer can currently claim is \$5.12 an hour, which, when combined with the required minimum cash wage of \$2.13 an hour, brings the total to \$7.25 an hour, meeting the FLSA requirement.

Tip regulations are complex, and over the last several years the details around tip regulations have changed several times. The Wage and Hour Division (WHD) of the DOL established what is known as the [80/20 rule](#) in the [Field Operations Handbook](#) to regulate when employers could claim a tip credit. The rule determined that employers could not claim a credit if their tipped employees spent more than 20 percent of their time doing untipped work. Take a waitress, for example, who in addition to working in her tipped capacity of tending to customers also cuts lemons for water, helps with closing, or makes coffee. If activities like these, those that do

not generate any tips, exceed 20 percent of her overall time, then her employer cannot claim a tip credit for her. The 80/20 rule necessitated close tracking of hours spent doing tippable work and created confusion over which activities were included in the realm of tip-generating work. The rule was temporarily rescinded in 2009 by a [WHD opinion letter](#) until it withdrew the opinion three months later, leaving 80/20 in effect. A [WHD opinion letter](#) in November of 2018 cemented 80/20 as an official WHD ruling. It wasn't until [February of 2019](#) that the WHD issued an amendment to their Field Operations Handbook to remove the 80/20 rule.

While the DOL lacked clarity in specifying when an employer could claim a tip credit, it remained fairly consistent on who could participate in tip-sharing arrangements. Since 1974, the DOL has only allowed employer-mandated tip pools to include tipped employees, excluding other workers who likely contribute to the success of tipped workers. Under these regulations, the waitress at the restaurant is able to pool and share her tips with her fellow waitstaff at the end of the shift, but the back-of-house employees, such as dishwashers, would be ineligible to receive any tip money from the mandatory pool. In 2011, the DOL continued to uphold this restriction regardless of whether the employer used a tip credit.

The recent proposed change from the DOL affects how employers claim a tip credit and who can participate in tip pools.

Department of Labor's Proposed Rule

The DOL's [proposed rule](#) amends tip regulations to align with [recent congressional action](#) and codifies changes concerning tip credit application. The DOL's proposed rule rescinds the 80/20 rule and determines tip-credit eligibility on the basis of whether the occupation is tipped or non-tipped, rather than time spent on tip-generating work. Regardless of how much time is spent cleaning tables, cutting lemons, and opening or closing the restaurant, the waitress who makes more than \$30 a month in tips could be paid the FLSA required minimum \$2.13 an hour cash wage by her employer. Discarding the 80/20 rule would not affect businesses who do not take a tip credit and pay all their employees the full minimum wage.

Employers may continue to choose to pool employee tips. Under the proposed rule, however, non-tipped employees such as dishwashers and cooks would be eligible for inclusion in the tip pool on the condition that the employer is not taking a tip credit. As a result of the proposed rule, under employer-created tip pooling arrangements, the employer could choose to include non-tipped workers. The new rule will not prevent tip pooling among only tipped employees in a situation where the employer takes a tip credit, nor will it affect any voluntary tip pooling among employees.

Along with tip pool and 80/20 changes, the rule makes clear that employers are not to pocket employee tips for any reason, and it includes a fine of \$1,100 per violation.

Implications

The effects of these new rule changes will vary [state-by-state](#) due to differences in state law pertaining to minimum wage and tip credit amount. Seven states require that employers pay tipped employees full state minimum wage, meaning that no tip credit would ever be taken. 26 states and the District of Columbia require a higher minimum cash wage than the \$2.13 an hour that the FLSA requires. In states where employers can take a tip credit, the rescension of the 80/20 rule would relieve employers of the burden to track the non-tip generating activities and time spent and could reduce instances of accidental FLSA violations.

Some have raised [concerns](#) about employers assigning excessive non-tip generating work and potentially reducing overall wages as a result. The extent to which employers would have their tipped workers doing other work is unclear.

The changes to tip sharing would allow for employees who previously did not have access to tips now to make above their standard hourly wage. On the flip side, the inclusion of more individuals in the tip pool could reduce the average amount each employee will receive.

The proposed rule was published to the [Federal Register](#) on October 8 and will be open for comment until December 9.