



Don't Get Soaked by Tip Pooling: Key Tip Pooling Issues for Employers

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One wage and hour issue that has received significant attention over the last few years is the legality of “tip pooling.” Tip pooling is generally the practice of collecting tips and redistributing them among eligible staff. The Biden Administration’s Department of Labor (DOL) has issued a final rule (the Rule) which becomes effective November 23, 2021, and which impacts tip pools and the circumstances under which managers and supervisors can — and perhaps more importantly can’t — keep tips they receive. The Rule also imposes penalties for the improper withholding of employees’ tips and allows employers to include back-of-house employees in tip pooling arrangements in certain circumstances.

Summary of Recent Developments on Tip Regulations

The Fair Labor Standards Act (FLSA) prohibits employers from participating in tip pools. The FLSA also allows certain employers to apply a limited amount of tips received by employees as a credit toward the employer’s obligation to pay minimum wage. Such credits are known as “tip credits.”

Under the FLSA, an “employer” includes “any person acting directly or indirectly in the interest of an employer in relation to an employee.” While this is an expansive definition, historically many courts were unwilling to apply the definition to persons such as lower-level supervisors who might technically fall under the definition but against whom it would be unreasonable to impose personal liability for FLSA violations. Instead, many courts looked at the economic reality of the employment relationship to determine if a particular employee was in fact an “employer” under the FLSA.

In 2018, Congress passed a law known as the Consolidated Appropriations Act (CAA) which amended the FLSA. Among the changes the CAA made was to expressly prohibit “managers or supervisors” from retaining tips “for any purposes” regardless of whether an employer took a tip credit. This change, on its face, broadened the group of employees who are prohibited from participating in tip pools. The CAA also granted the DOL the discretion to impose civil money penalties (CMPs) of up to \$1,100 (as adjustable for inflation) when employers unlawfully retained tips. In December 2020, the DOL issued a rule which sought to implement these changes made by the CAA.

On September 24, 2021, the Biden Administration issued a new rule which becomes effective November 23, 2021, and which has revised and delayed portions of the 2020 tip rule in important ways. One of the key provisions of the Rule specifies the certain instances where managers and supervisors may now lawfully keep tips that are given to them outside of tip pools. The Rule also provides definitions for “manager” and “supervisor,” which may make some of the earlier case law discussing those terms now obsolete. The Rule also permits employers who do not take a tip credit and who pay their tipped employees full minimum wage to establish tip pooling arrangements that include employees who do not customarily and regularly receive tips such as cooks, dishwashers, and custodians. In addition, the CMP which employers may face is adjusted for inflation up to \$1,162 per violation.

Managers and Supervisors May Now Keep Tips in Specified Situations

The Rule allows supervisors and managers to retain tips in limited situations. The Rule states that managers and supervisors are lawfully allowed to keep tips only if the tips are given as a result of work that the manager/supervisor “solely” and “directly” provided to the customer. This provision reflects the reality that managers and supervisors are sometimes called to fill in for shifts that would otherwise be filled by a tipped staff member such as a server or a bartender.

To clarify when supervisors or managers may keep tips, suppose a manager/supervisor was working a shift as a bartender and individually was taking orders and making drinks for customers sitting at the bar. In this scenario, the manager/supervisor could keep tips received from customers sitting at the bar that the manager/supervisor was serving because the manager/supervisor “directly” and “solely” serviced those customers by working alone.

However, if a manager/supervisor were helping deliver food to tables that were also being served by a server, the manager/supervisor could not keep any of the tips left by those customers because the manager/supervisor was not “solely” providing services to those customers. Thus, in order for a manager/supervisor to keep tips,

the services must be “directly” and “solely” provided by the manager/supervisor to the customer.

Definitions of “Manager” and “Supervisor”

Under the Rule and current regulations, a “manager” or “supervisor” is anyone: (1) whose primary duty is the management of the entire enterprise or of its customarily recognized subdivision or department; (2) who customarily and regularly directs the work of at least two employees; and (3) who has the right to fire or hire other employees or whose suggestions or recommendations regarding the hiring or firing of employees are given particular weight. Apart from that test, the DOL’s regulations state that a “manager” or “supervisor” also includes an individual who owns at least a bona fide 20% equity interest in the enterprise for which they are employed and who is actively engaged in the entity’s management.

Tip Pool Arrangements

Regarding tip pool arrangements, the Rule also states that an employer may require managers/supervisors to **contribute** tips they receive from their “direct” and “sole” services into a tip pool arrangement. However, managers/supervisors are always ineligible to **receive** any tips from a tip pool or sharing arrangement. There is no current exception to this requirement.

The Rule also states that employers may face a fine of up to \$1,162 for each instance that the DOL determines that an employer improperly withheld employee tips. Employers may face this fine regardless of whether they intended to wrongfully withhold tips and regardless of whether it was a one-time issue or a repeated violation. However, in calculating any penalty, the DOL must consider “the seriousness of the violations and the size of the employer’s business.”

Conclusion

The new Rule goes into effect on November 23, 2021. Employers in tipped industries, particularly those who have tip pools, should become familiar with the new requirements because they impose sizable penalties on employers who fail to comply. We encourage employers in tipped industries to consult with legal counsel on questions about how this Rule may affect their businesses.

This is the first of two articles discussing tip pools.

Disclaimer: This information is not intended to be legal advice. Rather, it seeks to make recipients aware of certain legal developments that affect human resource issues. Recipients who want legal advice concerning a particular matter should consult with an attorney who is given a full understanding of the relevant facts pertaining to the particular matter.

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