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Wage and Hour Division
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FIELD ASSISTANCE BULLETIN No. 2012-2

MEMORANDUM FOR: REGIONAL ADMINISTRATORS AND DISTRICT DIRECTORS

FROM:


NANCY J. LEPPINK
Deputy Administrator

SUBJECT: Enforcement of 2011 Tip Credit Regulations

The purpose of this memorandum is to advise staff that the Department of Labor's ("Department") new regulations addressing ownership of employee tips under section 3(m) of the Fair Labor Standards Act ("FLSA" or "Act"), 29 U.S.C. 203(m), should be enforced uniformly across the country, including in states covered by the Ninth Circuit. See 76 Fed. Reg. 18832, 18856 (Apr. 5, 2011).¹ The Wage and Hour Division will enforce nationwide the 2011 final rule explaining that a tip is the sole property of the tipped employee regardless of whether the employer takes a tip credit, and that the employer is prohibited from using an employee's tips, whether or not it has taken a tip credit, except as a credit against its minimum wage obligations to the employee, or in furtherance of a valid tip pool. The Wage and Hour Division will enforce the policy as articulated by this guidance prospectively in those states under the jurisdiction of the Ninth Circuit.

The new tip credit regulations, which became effective on May 5, 2011, incorporate Wage and Hour's longstanding position that the 1974 amendments to the FLSA established that tips are the property of the employee, and that an employer can use its employees' tips only in the limited ways prescribed by section 3(m) even when the employer has not taken a tip credit against its minimum wage obligations. See 29 C.F.R. 531.52. Prior to the publication of the 2011 tip regulations, the U.S. Court of Appeals for the Ninth Circuit issued a decision, Cumbie v. Woody Woo, Inc., 596 F.3d 577 (9th Cir. 2010), which held that section 3(m)'s limitations on an employer's use of its employees' tips do not apply when the employer does not take a tip credit.²

¹ The Ninth Circuit has appellate jurisdiction over the states of California, Nevada, Washington, Oregon, Alaska, Idaho, Montana, Hawaii, and Arizona.

² Although the U.S. Court of Appeals for the Third Circuit summarily affirmed a district court's decision in Platek v. Duquesne Club, 961 F. Supp. 831, 834 (W.D. Pa. 1995), aff'd without opinion, 107 F.3d 863 (3d Cir.) (Table), cert. denied, 522 U.S. 934 (1997), that also held that

As this Bulletin explains, because that decision was issued before the Department promulgated its new tip credit regulations, it does not preclude Wage and Hour from enforcing these regulations in those states covered by the Ninth Circuit.

History

The FLSA's tip credit provision was originally created through the 1966 amendments to the Act, and specifically permitted employers to credit a portion of their employees' tips against their minimum wage obligations. See Pub. L. No. 89-601, §101(a) (1966). In 1974, the tip credit provision was amended in pertinent part to add a requirement that tips received by the employee must be retained by the employee except through valid tip pooling arrangements among employees who customarily and regularly receive tips. See Pub. L. No. 93-259, §13, 88 Stat. 55 (1974). Immediately following the 1974 amendments to section 3(m), Wage and Hour explained that this new statutory language requiring employees to retain all tips was significant because it made absolutely clear "that an employer could not use the tips of a 'tipped employee' to satisfy more than 50 percent of the Act's applicable minimum wage," and that the amendments "would have no meaning or effect unless they prohibit agreements under which tips are credited or turned over to the employer for use by the employer in satisfying the monetary requirements of the Act." Opinion Letter, June 21, 1974. Wage and Hour also publicly stated that its tip credit regulations promulgated in 1967, which tacitly permitted employers and employees to agree to give the employer complete control over its employees' tips, were superseded by the 1974 amendments because they did not reflect the new statutory limitations, and that new regulations incorporating those amendments would be forthcoming. See Opinion Letter WH-310, 1975 WL 40934 (Feb. 18, 1975).³ Finally, the Department explicitly distinguished the state of the law in 1974 governing the payment of tipped employees with the law as it existed at the time that the Supreme Court decided Williams v. Jacksonville Terminal Co., 315 U.S. 386 (1942), explaining that "the situation of a tipped employee is far different" than it was at the time of that decision, when the FLSA did not provide for a tip credit and where the Court concluded that employer-employee agreements to share tips would be presumed valid "absent statutory interference." Opinion Letter WH-321, 1975 WL 40945 (Apr. 30, 1975). In light of the agency's view that the legislative history to the 1974 amendments clearly demonstrated Congress' intent to permit an employer to use its employees' tips only as specifically prescribed by section 3(m), Wage and Hour concluded that "[i]f an employer should elect not to avail himself of this limited exception [to pay the full minimum wage], he would have to pay his tipped employees in accordance with the Act's minimum wage standards and, in addition, allow them to keep their tips." Id.

A number of courts analyzing section 3(m) shortly after the 1974 amendments concurred with Wage and Hour's assessment of the new tip retention clause. "[W]e agree," the Fourth Circuit

3(m) restricts an employer's use of an employee's tips only when the employer has taken a tip credit, that decision is not discussed in this Bulletin because, as an unpublished decision, it does not have precedential value.

³ Despite this statement, the regulations were not revised to reflect the 1974 amendments until 2011, in the rulemaking referenced in this Bulletin.

wrote, that "tips belong to the employee to whom they are left." Richard v. Marriott Corp., 549 F.2d 303, 305 (4th Cir. 1977), cert. denied, 433 U.S. 915 (1977). The courts also rejected employers' arguments that they could use employee tips to fulfill 100% of their minimum wage obligations if they did not utilize a tip credit, stating that "this argument stands the amendment, particularly the 1974 one, on its head[;] [t]he amendments have accomplished nothing if defendants argument is accepted." Usery v. Emersons Ltd. et al., 1976 WL 1168, at *4 (E.D. Va. 1976), vacated & remanded on other grounds sub. nom. Marshall v. Emersons Ltd., 593 F.2d 565 (4th Cir. 1979); see Marriott, 549 F.2d at 305 ("It is nonsense to argue . . . that compliance with the statute results in one-half credit, but that defiance of the statute results in 100 percent credit."). These decisions, issued just a few years after the 1974 amendments to section 3(m), recognized that an employer would have no reason to use the tip credit as a partial credit against its minimum wage obligations if it could use all of its employees' tips to fulfill its entire minimum wage obligation to the tipped employees or other employees. In other words, if there are no restrictions on an employer's use of its employees' tips when it does not utilize a tip credit, the employer can institute a mandatory tip pool that requires employees to contribute all their tips and receive only sufficient tips back to meet the minimum wage, or even without a tip pool, can mandate that employees turn over all their tips and use those tips to pay them the minimum wage.

Ninth Circuit's Decision in *Cumbie v. Woody Woo, Inc.*

Prior to the promulgation of the 2011 tip credit rules, the Ninth Circuit issued a decision which concluded that the text of section 3(m) itself does not impose any restrictions on an employer's use of its employees' tips when the employer has not taken a tip credit. See Woody Woo, 596 F.3d at 579. The employer in Woody Woo was prohibited by state law from taking a tip credit, and paid its employees the full minimum wage, but required its tipped employees to participate in a tip pool that included dishwashers and cooks, individuals who do not "customarily and regularly receive tips" under the terms of the statute. The tipped employee brought suit alleging a violation of the FLSA because she did not receive the full minimum wage plus all tips received.

The Ninth Circuit stated that the Supreme Court's 1942 decision in Jacksonville Terminal established a "default rule that an arrangement to turn over or to redistribute tips is presumptively valid," and that this rule was presumed to be in effect absent "statutory interference." Woody Woo, 596 F.3d at 579 (citing Jacksonville Terminal, 315 U.S. at 397). After analyzing the text of section 3(m), the court concluded that it is "clear" that that provision disrupts the Jacksonville Terminal default rule only when a tip credit is taken, because the last sentence of section 3(m), providing that an employer cannot take a tip credit unless it has provided notice and permits employees to retain all their tips (except for a valid tip pool), "imposes *conditions* on taking a tip credit and does not state freestanding *requirements* pertaining to all tipped employees." Id. at 580. The Ninth Circuit therefore did not read section 3(m) itself as imposing any limitations on the use of an employee's tips when a tip credit is not taken. The Ninth Circuit concluded its decision in Woody Woo with the statement that where "nothing in the text of the FLSA purports to restrict employee tip-pooling arrangements when no tip credit is taken, we perceive no statutory impediment to Woo's practice." Id. at 583.

2011 Final Rule

The Department's 2011 final rule amending its tip credit regulations specifically sets out Wage and Hour's interpretation of the Act's limitations on an employer's use of its employees' tips when a tip credit is not taken. Those regulations state in pertinent part:

Tips are the property of the employee whether or not the employer has taken a tip credit under section 3(m) of the FLSA. The employer is prohibited from using an employee's tips, whether or not it has taken a tip credit, for any reason other than that which is statutorily permitted in section 3(m): As a credit against its minimum wage obligations to the employee, or in furtherance of a valid tip pool.

29 C.F.R. 531.52. These regulations fill a gap in the statutory scheme left by the Act's silence on the use of employees' tips when no tip credit is taken. See, e.g., Barnhart v. Walton, 535 U.S. 212, 218 (2002) ("[S]ilence, after all, normally creates ambiguity. It does not resolve it."); Senger v. City of Aberdeen, SD, 466 F.3d 670, 672 (8th Cir. 2006) (recognizing Department's authority to fill a "gap" in the FLSA's regulatory scheme). Nothing in Woody Woo, which addressed the regulatory scheme as it existed at the time of the decision, precludes the agency from filling this gap with its legislative rules promulgated pursuant to specific congressional authorization and after notice and comment. See, e.g., Nat'l Cable & Telecomm. Assoc. v. Brand X, 545 U.S. 967, 982 (2005) ("A court's prior judicial construction of a statute trumps an agency construction otherwise entitled to *Chevron* deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion."); Garfias-Rodriguez v. Holder, 649 F.3d 942, 947-48 (9th Cir. 2011). Furthermore, because these gap-filling rules are legislative, they have the force of law, and are "binding upon all persons, and on the courts, to the same extent as a congressional statute." Nat'l Latino Media Coalition v. Federal Commc'ns Comm'n, 816 F.2d 785, 788 (D.C. Cir. 1987); see Miller v. California Speedway Corp., 536 F.3d 1020, 1033 (9th Cir. 2008) ("[L]egislative rules 'create rights, impose obligations, or effect a change in existing law pursuant to authority delegated by Congress.'" (citation omitted)). They therefore create the equivalent of the "statutory interference" necessary to invalidate the Jacksonville Terminal default rule that employers and employees can agree to share tips.