FLSA: THE TIP CREDIT

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While the Fair Labor Standards Act (FLSA) allows employers to pay employees less than minimum wage (currently $5.15 per hour) in certain circumstances, employers must first satisfy all statutory and regulatory requirements before permitting anyone to work for less than minimum wage.

FLSA section 203 allows employers to credit the tips a tipped employee receives against the minimum wage. The Code of Federal Regulations (CFR) defines a tip as an amount "presented by a customer as a gift or gratuity in recognition of some service performed for him." Gifts other than money, such as merchandise, are not tips. The FLSA allows a separate credit for employer-provided meals and lodging. According to the 29 USC section 203(t), a "tipped employee" works "in an occupation in which he customarily and regularly receives more than $30 a month in tips." Where an employee performs more than one function, one or more of which are in a position where she does not customarily and regularly receive $30 in tips per month, the employer can use the tip credit only for time spent performing tipped work.

The FLSA permits employers to pay a tipped employee cash wages of $2.13 per hour, provided the employee's gross compensation (tips plus cash wages) equals at least the minimum wage. New York Labor Law section 652(4), however, requires a higher cash wage for many occupations.

Before claiming credit for tips received by a tipped employee, an employer must first meet two conditions:

- The employer must explain it to the employee in advance; and
- The employee must retain all tips she receives.

The second condition has two exceptions:

- Employees that "customarily and regularly receive tips" may pool their tips, and
- Employers may reduce tips paid by credit card to reflect the fee charged by the credit card company.

BEFORE CLAIMING CREDIT FOR TIPS RECEIVED BY a tipped employee, an employer must first explain it to the employee in advance; and the employee must retain all tips she receives.

Illustrative Cases

Kilgore v. Outback Steakhouse of Florida, Inc. [160 F.3d 294, 4 WH Cases 2d 1729 (6th Cir. 1998)] is the leading case on the tip credit. Among other things, the plaintiff class claimed that Outback failed to inform them of the tip credit. The court disagreed, holding that an employer must merely inform employees of its "intent to take a tip credit," not explain it. The court also held that the FLSA does not limit the amount of tip-out (the amount servers have to share with other employees) to a customary or reasonable amount.

The plaintiffs also challenged the restaurant's inclusion of hosts in the tip pool; the court upheld Outback's policy. The plaintiffs' argument that hosts are not tipped employees failed because Department of Labor regulations indicate that tips received from a tip pool should be considered tips for the purpose of 29 USC sections 203(m) and (t), and because hosts at Outback are part of an occupation that customarily and regularly receives tips. Hosts "sufficiently interact with customers in an industry (restaurant) where undesignated tips are common." Noting that hosts greeted guests, seated them, gave them menus, and "enhanced" their wait, the court distinguished them from "employees like dishwashers, cooks, or ... janitors who do not directly relate with customers at all." (See also *Dole v. Continental Cuisine, Inc.* [751 F. Supp. 799 (E.D. Ark. 1990)], in which a maitre d' lawfully participated in a tip pool; and *Harnett v. Wade-Mark Eleven, Inc.* [156 A.D. 2d 559 (2d Dept 1989)], which found tip pooling to be lawful where completely voluntary, administered by employees, and management did not retain any of the tips.)

In contrast, in *Ayres v. 127 Restaurant Corp.* [12 F. Supp. 2d 305 (S.D.N.Y. 1998), aff'd, 201 F.3d 430 (2d Cir. 1999)], the court held that the defendant improperly included the restaurant's general manager in the tip pool, because managers do not customarily and regularly receive tips. The court also found the violation willful, extending the statute of limitations from two to three years. A number of other decisions may also be of interest. In *King v. Friend of a Farmer Corp.* [2001 U.S. Dist. Lexis 10630 (S.D.N.Y. July 25, 2001)], the defendant's motion for summary judgment was denied where plaintiff alleged defendant took funds from the tip pool "to balance the cash register." The court in *Zhao v. Benihana, Inc.* [2001 U.S. Dist. Lexis 10678 (S.D.N.Y. July 5, 2001)] authorized notice to potential class members where the plaintiff alleged the defendant required servers to share tips with kitchen helpers and did not inform servers about the tip credit. The defendant violated FLSA by taking tip credit without informing plaintiff in *Cao v. Chandara Corp.* [2001 U.S. Dist. Lexis 8631 (S.D.N.Y. June 27, 2001)]. Finally, in *Realite v. Ark Restaurants Corp.* [7 F. Supp. 2d 303 (S.D.N.Y. 1998)], the plaintiffs claimed that the defendant required improper tip pooling and failed to explain the tip credit. ❑

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