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DOL Issues New Tip Regulations Under the Fair Labor Standards Act

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The Department of Labor (“DOL”) announced a final rule revising its tipped employee regulations to address changes to section 3(m) of the Fair Labor Standards Act (“FLSA”) made by the Consolidated Appropriations Act of 2018 (“CAA”).¹ The CAA made several notable changes to the FLSA, including prohibiting managers and supervisors from participating in tip pools, clarifying tip credits for employees working dual jobs, and imposing new civil penalties on employers that unlawfully retain employees’ tips. The DOL final rule implements and codifies those changes, but also rescinds the Department’s so-called “80/20 rule” that required employers to pay a tipped employee the full minimum wage, rather than the lower cash wage applicable to tipped employees, if the employee spent more than 20% of his or her time performing allegedly non-tipped duties. The final rule will become effective on March 1, 2021.²

We summarize the key changes made by the DOL final rule below.

Managers and Supervisors Cannot Participate in a Tip Pool

The CAA added language to the FLSA prohibiting employers from retaining their employees’ tips “for any purposes, including allowing managers or supervisors to keep any portion of employees’ tips, regardless of whether or not the employer takes a tip credit.” 29 U.S.C. § 203(m)(2)(B). The DOL final rule incorporates that change by confirming that managers and supervisors cannot receive employees’ tips as part of any tip pooling arrangement.

The final rule also provides guidance to employers to help determine whether an employee constitutes a manager or a supervisor. Specifically, the final rule uses the “duties test” from the FLSA’s executive-employee exemption. Under this test, the DOL will consider an employee a manager or a supervisor if:

1. The employee’s primary duty is managing the enterprise or a customarily recognized department or subdivision of the enterprise;
2. The employee customarily and regularly directs the work of at least two or more other full-time employees or their equivalent; and
3. The employee has the authority to hire or fire other employees, or the employee’s suggestions and recommendations as to the hiring or firing are given particular weight.

The DOL's definition of a manager or supervisor also includes any individual who owns at least a bona fide 20% equity interest in the enterprise in which the individual is employed and actively engaged in its management.

Employees Who Do Not "Customarily and Regularly" Receive Tips May Participate in Tip Pools, So Long As No Tip Credit Is Taken

Previously, DOL regulations provided that employers could not include employees who did not customarily and regularly receive tips (e.g., cooks and dishwashers) in a mandatory tip pool. Congress suspended portions of these regulations in the CAA. The DOL final rule specifies that employers may include employees who do not customarily and regularly receive tips in a tip pool, so long as the employer does not take a tip credit towards minimum wage requirements.

The "80/20 Rule" Is Formally Eliminated

The dual jobs regulation addresses when an employer may take a tip credit towards minimum wage requirements for time that an employee spends performing duties that do not directly result in tips for that employee. Previously, the DOL employed the "80/20 rule" in such cases. That rule required employers to pay tipped employees the full minimum wage, rather than the lower cash wage applicable to tipped employees, for non-tipped duties if the employee spent more than 20% of his or her time performing non-tipped duties.

The DOL final rule formally abolishes the "80/20 rule" in favor of a new two-factor test. The final rule provides that an employer may take a tip credit for time that an employee spends performing related, non-tipped duties if two circumstances are satisfied:

1. The duties must be related to the employee's tipped occupation; and
2. The employee must perform the related duties contemporaneously with the tip-producing activities or within a reasonable time immediately before or after the tipped activities.

The DOL will presume that a non-tipped duty is "related" to the employee's tipped occupation if it is listed as a task of the tip-producing occupation in the Occupational Information Network ("O*NET"), available at www.onetonline.org. However, the list of tasks in the O*NET is not exclusive.

One benefit of this new test is that, unlike the "80/20 rule," the new test does not entail a minute-by-minute accounting of tipped employees' work to ensure that non-tipped related work does not exceed a quantitative cap. Each employee can instead perform the related, non-tipped work of his or her tipped occupation as needed in conjunction with his or her tipped work—either contemporaneously with or for a reasonable time immediately before or after the tipped work—and employers may take a tip credit without precisely tracking the time spent by the employee as he or she moves between duties.

New Recordkeeping Requirements for Employers That Do Not Take a Tip Credit

The DOL final rule requires employers that operate a mandatory tip pool to maintain and preserve records:

1. identifying each employee who receives tips; and
2. containing the weekly or monthly amount of tips received for each employee, as reported by the employee to the employer (this may consist of reports from the employees to the employer on IRS Form 4070).

New Notice Requirements for Employers That Take Tip Credits

The DOL final rule mandates that employers inform tipped employees in advance of the employer's use of a tip credit. Specifically, the employer must provide notice to tipped employees of the following:

- The amount of the cash wage that is to be paid by the employer;
- The additional amount by which the wages of the tipped employee will be considered increased on account of the tip credit claimed by the employer, which amount may not exceed the value of the tips actually received by the employee;
- That all tips received by the tipped employee must be retained by the employee except for a tip pooling arrangement; and
- That the tip credit shall not apply to any worker who has not been informed of these requirements in this section.

New Rule Regarding Redistribution of Tips

The DOL final rule requires employers that collect tips to facilitate a mandatory tip pool to fully redistribute the tips no less often than when they pay wages to avoid "keep[ing]" the tips in violation of the FLSA. 29 U.S.C. § 203(m)(2)(B). If that is not possible, the employer must distribute the tips as soon as practicable.

Civil Penalties for Violations

The DOL final rule provides that employers that retain any portion of the tips received by their employees for any purposes shall be subject to a civil penalty not to exceed \$1,100 per violation, in addition to being liable to the employee for all tips unlawfully kept, and an additional equal amount as liquidated damages. The DOL's current policy is to assess such penalties only in instances of repeated and willful violations of the law.

Practical Considerations

Employers should review and evaluate their tip-pooling and tip-credit arrangements in light of the DOL's final rule. Employers who do not take a tip credit may now enjoy the increased flexibility of being able to include employees who do not customarily and regularly receive tips (e.g., cooks and dishwashers) into their tip pool. However, these employers must also comply with new recordkeeping requirements. Employers who do take a tip credit should consider the DOL's changes to the dual jobs regulation and consider whether their use of a tip credit is appropriate under the revised regulations. These employers should also be cognizant of the DOL's new notice requirements for employers who take a tip credit.

Monitor Future Developments

The final rule will become effective on March 1, 2021. However, because the final rule goes into effect after the Biden inauguration, employers should be aware that some or all of these changes may be blocked before their implementation. Additionally, the Biden administration may promulgate new rules that affect employers' tip practices. President-Elect Biden has indicated, for example, that he intends to eliminate the tip credit altogether.³ Employers, therefore, should closely monitor developments in this area in the coming months.

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- ¹ State law regarding tipped employees, and whether an employer can take a tip credit against minimum wage, varies by state. The FLSA, however, sets forth the basic protections that must be afforded to all employees.
 - ² It bears noting that, once the final rule is reported to Congress, it will trigger the period for potential Congressional review (and disapproval) under the Congressional Review Act. 5 U.S.C. §§ 801 *et seq.* Therefore, employers should closely monitor future developments in this area.
 - ³ <https://joebiden.com/empowerworkers/>.

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