RESPONSE TO NOTICE OF PROPOSED RULEMAKING

AND REQUEST FOR COMMENTS REGARDING

TIP REGULATIONS UNDER THE FAIR LABOR STANDARDS ACT

(RIN 1235-AA21)

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I. INTRODUCTION

We offer the following in response to the U.S. Department of Labor's Notice of Proposed Rulemaking (NPRM) with respect to "Tip Regulations Under the Fair Labor Standards Act (FLSA)" published on December 5, 2017 at 82 Fed. Reg. 57395, Regulatory Information Number (RIN) 1235–AA21.

By way of background, Fisher & Phillips LLP is a national law firm that has been engaged in the practice of labor and employment law for nearly 75 years. Throughout that time, an extensive portion of our practice has included statutory and regulatory analysis, interpretation, compliance-counseling, dispute resolution, and the presentation of commentary as to matters relating to the FLSA in particular.

For 30 years, our activities in these respects were guided by Henry A. Huettner, who, prior to joining the firm, had been Regional Director for USDOL's Southeastern Region. He was first employed by the Wage and Hour Division as an Investigator in 1941. The firm's remarks on the FLSA and related regulations are significantly influenced by Mr. Huettner's substantive and historical knowledge, as well as his experiences in enforcing and interpreting this law, all of which provide a foundation for the current-day views of the firm's expert practitioners.

The USDOL now invites comments regarding its proposal to rescind portions of regulations published at 76 Federal Register 18832 (April 5, 2011) regarding tips and, in particular, the imposition of "restrictions on employers that pay a direct cash wage of at least the full federal minimum wage and do not seek to use a portion of tips as credit toward their minimum wage obligations." 82 Fed. Reg. 57395. Before we turn to the NPRM itself, we find it necessary to summarize the relevant historical background, which establishes that the NPRM is a correction rather than a revision given that the 2011 regulations were unauthorized.

II. HISTORICAL BACKGROUND PRECEDING 2011 REVISIONS

The FLSA was enacted in 1938. In its original form, however, it did not address the issue of tips; to whom the tips belong, whether the tips constitute wages, or related questions. In 1942, the Supreme Court took up the issue of tips in *Williams v. Jacksonville Terminal Co*., 315 U.S. 386, 62 S.Ct. 659, 86 L.Ed. 914 (1942). In *Jacksonville Terminal*, the Court set forth the principle that "[i]n businesses where tipping is customary, the tips, *in the absence of an explicit contrary understanding*, belong to the recipient. Where, however, [such] an arrangement is made…, in the absence of statutory interference, no reason is perceived for its invalidity." *Jacksonville Terminal*, 315 at 397 (emphasis added). Interpreting this language, courts have construed *Jacksonville Terminal* as establishing a "default rule" that, when the tip credit is not applied, "an arrangement to turn over or to redistribute tips is presumptively valid" for FLSA purposes. *See Crumbie v. Woody Woo, Inc*., 596 F.3d 577, 579 (9th Cir. 2010).

In 1966, Congress amended the FLSA to provide for the first time, within section 3(m)'s definition of a "wage," that an employer could utilize a limited amount of its employee's tips as a credit against its minimum wage obligations to that employee through a so-called "tip credit." *See Updating Regulations Issued Under the Fair Labor Standards Act*, 76 Fed. Reg. 18832-01, 18838 (April 5, 2011). Notably, Congress' introduction of the tip credit was responsive to tip practices that were already in existence.

In 1974, Congress again amended the FLSA's Section 3(m), and more fully established the contours of the "tip credit," although that phrase has never actually appeared in Section 3(m). The 1974 Amendments established that there are two components of the employer's wage obligation to an employee for whom the employer takes the tip credit: (1) the employer's cash wage obligation and (2) "an additional amount on account of the tips received by such employee." 29 U.S.C. § 203(m). The combination of the two must equal at least the federal minimum wage. Congress also made clear that the "additional amount on account of tips may not exceed the value of the tips actually received by an employee." *Id.*

At the same time, *and for the first time*, Congress also addressed the concept of "tip pooling." After setting forth the employer's wage obligations for tipped employees, when relying on the tip credit, Congress added two additional requirements. First, employers are required to provide prior notice of their intent to use a tip credit. Second, Congress required that "all tips received by such employee shall have been retained by the employee, except that this subsection shall not be construed to prohibit the pooling of tips among employees who customarily and regularly receive tips." 29 USC § 203(m). This is Congress' only reference to "tip pooling" within the FLSA.

The single reference to "tip pooling" came within the specific context of Congress setting forth the conditions imposed upon an employer who seeks to utilize the Section 3(m) "tip credit." Said differently, Congress decided to establish parameters for a permissible tip pooling arrangement (*i.e.* "the pooling of tips among employees who customarily and regularly receive tips") only with respect to a particular class of employees: those employees for whom an employer takes the tip credit. *See Oregon Rest. And Lodging Ass'n. v. Perez*, 843 F.3d 355, 360 (9th Cir. 2016) (O'Scannlain, J., dissenting). While Congress could have established parameters for "tip pooling" arrangements outside the context of the tip credit, it did not do so (and never has). There have been no subsequent amendments to the FLSA that have addressed ownership of tips or tip pooling arrangements.

Thus Congress has addressed the ownership of tips (and tip pools) in only one specific statutory provision: Section 3(m) of the FLSA. If an employer takes the Section 3(m) tip credit, the tips belong to the receiving employee with the limited exception that permits an employer to require that such tips be contributed to a "pooling of tips among employees who customarily and regularly receive tips." Outside of these limited circumstances, the *FLSA* does not regulate tip ownership.

We urge USDOL to take this background into account as it moves forward. In particular, the 2011 rulemaking should not be its point of departure.

III. THE STATUTORY LANGUAGE IS LIMITED

If the employer does not take the tip credit, and the parties have established an understanding that some or even all tips belong to the employer, the employee has no legal claim to those tips. Nothing in the plain language of the statute supports a contrary conclusion.

In its simplest terms, *Jacksonville Terminal* has never been overruled or abrogated, whether by subsequent judicial decision or by Congressional legislation. 315 U.S. 386 (1942)(employer and employees could agree that the employer could take the "compensation paid by the [customers]", whether a fixed charge or a tip; FLSA did not prohibit transferring tips to the employer's credit). *See Cumbie v. Woody Woo*, 596 F.3d 577, 582 (9th Cir. 2010)("we have . . . determined [that Section 3(m)] does not alter the default rule in *Williams* that tips belong to the servers to whom they are given only 'in the absence of an explicit contrary understanding' that is not otherwise prohibited." [Citation omitted]). As a result, its "default rule" remains in effect. Where an arrangement exists that tips received by the employee will be relinquished to the employer, for any purpose, such an arrangement is valid. Congress has passed no further laws addressing this issue, so there is no "statutory interference" within Section 3(m) or any other provision within the FLSA.

In 2011, the USDOL under the prior Administration took the position that the 1974 section 3(m) amendments regarding tip pooling were intended to prohibit such agreements. *See* S. Rep. No. 93–690, at 43 (1974)('The [retention requirement] is added to make clear the original Congressional intent 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.'). 76 Fed.Reg. 18839. It stated that the regulations (as they stood before and after 1974), which allowed an employer to require employees to turn over all their tips to the employer, were superseded by the statutory amendment restricting an employer's ability to utilize an employee's tips to satisfy its minimum wage obligation. *Id*.

Again, that is not supported by a plain reading of the statute as actually amended. Ultimately, the assertion that Section 3(m) precludes a non-tip-credit-taking employer from exercising dominion over tips is predicated upon select legislative history from years after the credit was introduced. Further, to the extent that this view has been expressed in USDOL opinion letters and other statements of policy issued since the 1974 amendments based upon that history, it is similarly unfounded. *See*, *e.g.*, 76 Fed.Reg. 18839, 18841 (citing for support to Senate committee reports, *i.e.*, S. Rep. No. 93-690 (1974) and S. Rep. No. 95-440 (1977)). USDOL's opinions and other position statements improperly supported carry no independently-based weight simply because of their numerosity.

This is also true of the 1976 and 1977 cases that USDOL cited in this respect in 2011, that is, *Richard v. Marriott Corp*., 549 F.2d 303 (4th Cir. 1977), *cert. den*., 433 U.S. 915 (1977) and *Usery v. Emersons Ltd*., 22 W.H. Cases 1437 (E.D. Va. 1976), *vacated and remanded on other grounds*, 593 F.2d 565 (4th Cir. 1979). 76 Fed.Reg. 18841 (April 5, 2011). Both courts relied in significant part upon the 1974 Senate committee report.

IV. STATUTORY LANGUAGE CONTROLS, NOT LEGISLATIVE HISTORY

If a court is able to discern a statute's meaning from the language of the provision itself, then legislative history plays no role. *See*, *e.g.*, *Ratzlaf v. United States*, 510 U.S. 135, 147-48 (1994)("we do not resort to legislative history to cloud a statutory text that is clear."). *See also Barnhill v. Johnson*, 503 U. S. 393, 401 (1992) (appeals to legislative history are well taken only to resolve statutory ambiguity).

Multiple courts and judges have concluded that Section 3(m) is clear on its face insofar as its limitation to tip-credit-taking employers is concerned. *See*, *e.g.*, *Marlow v. The New Food Guy, Inc.*, 861 F.3d 1157 (10th Cir. 2017)(such that "there is no call for us to review legislative history"); *Cumbie v. Woody Woo*, *supra*; *Aguila v. Corp. Caterers II, Inc.*, 26 W.H. Cases2d 1516 (S.D. Fla. 2016); *Brueningsen v. Resort Express Inc.*, 2015 W.H. Cases2d 17521 (D. Utah 2015); *Stephenson v. All Resort Coach, Inc.*, 2013 WL 4519781 (D. Utah 2013). *See also Oregon Restaurant and Lodging Ass'n. v. Perez*, 843 F.3d 355 (9th Cir. 2016)(O'Scannlain, J., dissenting); *Oregon Restaurant and Lodging Ass'n. v. Perez,* 816 F.3d 1080 (9th Cir. 2016)(Smith, J., dissenting).

The plain language of Section 3(m) is not the only evidence showing that Congress did not seek to establish a blanket rule regarding the validity of "tip pools". The legislative history (if of any relevance at all) to the 1974 Amendment further demonstrates that Congress sought to impose parameters on "tip pooling arrangements" only with respect to the tip credit. "An employer will lose the benefit of the [tip credit] exception if tipped employees are required to share their tips with employees who do not customarily and regularly receive tips." S. Rep. No. 93-690, at 43 (1974). Thus, even the 1974 Senate report is ambiguous and internally inconsistent. *See*, *e.g.*, *Oregon Restaurant and Lodging Ass'n. v. Perez*, *supra*, 843 F.3d at 1708)(O'Scannlain, J., dissenting):

> The very Senate Committee Report the majority relies on explains that an "employer will lose the benefit of [the tip credit] exception if tipped employees are required to share their tips with [non-tipped] employees". *Or. Rest.*, 816 F.3d at 1089 (quoting S. Rep. No. 93-690, at 43 (1974)). That statement makes sense only on the assumption that employers who forgo the tip credit *can* require tip pooling among customarily and non-customarily tipped employees, just as *Cumbie* had said. All the majority can muster in response is a more general statement from the same report that § 203(m) "requir[es] . . . that all tips received be paid out to tipped employees." *Id*. at 1090. That's it. Even fans of legislative history should hold their noses before allowing one vague statement from one committee report to trump not only the clear text of the statute, *but also the express interpretation of that text as set out in the very same report*.

[Insertion, ellipsis, and emphasis in original].

The 1977 report has even *less* standing. It was not contemporaneous with the consideration or passage of the relevant 1974 Section 3(m) amendments. It simply represents the later ruminations of a committee of a *different* Senate.

Cumbie, which is still good law, rejected head-on the proposition that taking all of the tips to fund employee wages unlawfully circumvents Section 3(m):

> Finally, Cumbie argues against the result we reach because "[a]s a practical matter, it nullifies legislation passed by Congress." Her argument, as we understand it, is that Woo is functionally taking a tip credit by using a tip-pooling arrangement to subsidize the wages of its non-tipped employees. The money saved in wage payments is more money in Woo's pocket, which is financially equivalent to confiscating Cumbie's tips via a section 203(m) tip credit (with the added benefit that this 'de facto' tip credit allows Woo to bypass section 203(m)'s conditions).
>
> Even if Cumbie were correct, "we do not find [this] possibility . . . so absurd or glaringly unjust as to warrant a departure from the plain language of the statute." The purpose of the FLSA is to protect workers from "substandard wages and oppressive working hours." Our conclusion that the FLSA does not prohibit Woo's tip-pooling arrangement does not thwart this purpose. Cumbie received a wage that was far greater than the federally prescribed minimum, plus a substantial portion of her tips. Naturally, she would prefer to receive all of her tips, but the FLSA does not create such an entitlement where no tip credit is taken. Absent an ambiguity or an irreconcilable conflict with another statutory provision, "we will not alter the text in order to satisfy the policy preferences" of Cumbie and amici.

Cumbie v. Woody Woo, *supra*, 596 F.3d at 582-83.

Overall, if Congress wanted the FLSA to address the retention of tips in a more general sense, it should have done so in the text of the statute in 1966 or even 1974. It did not, and as such the USDOL's regulations cannot afford protection to tips that are not within the scope of the FLSA.

V. ALL NON-TIP CREDIT ARRANGEMENTS ARE OUTSIDE THE FLSA

The NPRM primarily focuses on an employer's ability to require tipped employees to share their tips with non-tipped employees. The principles that limit the Agency's ability to restrict an employer in such circumstances, however, apply to all circumstances in which no tip credit is taken and an employer exercises control over tips in some manner.

Either Section 3(m) applies even in the absence of a tip credit, or it doesn't; there *is no* in-between. One thing that is entirely clear from the 1974 version of Section 3(m) (and, to the extent that it is relevant, from the 1974 Senate Committee Report) is that, if Section 3(m) applies, then it is impermissible to require tipped employees to share tips with non-tipped employees. Inasmuch as USDOL has concluded that Section 3(m) *permits* such a sharing of tips if the employer takes no tip credit, this can only be sustained in light of an at-least-implicit, more-general principle that Section 3(m) does not apply *at all* if the employer takes no tip credit. The state-of-play reverts to the one articulated in *Jacksonville Terminal* as discussed above.

Indeed, this Agency recognizes that, "[t]o the extent employers may otherwise make an arrangement to allocate any customer tips *to make capital improvements to their establishments (e.g., enlarging the dining area to accommodate more customers), lower restaurant menu prices*, provide new benefits to workers (*e.g.*, paid time off), increase work hours, or hire additional workers, these are also potential benefits to employees and the economy overall that may result under the proposed rule." Section VII, Subsection C, "Discussion of Benefits and Other Potential Impacts of the Proposed Rule", 82 Fed.Reg. 57408(emphasis added). The enumerated benefits, particularly those emphasized here, would be consistent with the FLSA only if Section 3(m) does not apply.

It must therefore surely be the case that, if an employer can take tips to make capital improvements, for example, then taking tips so as to "allocate" them to wages is also permitted. There could be no legitimate or meaningful distinction between an employer's deciding to take employees' tips for its exclusive benefit having a non-wage-payment character versus management's doing so for the *express purpose* of wage payment. The bottom line is that an employer can exercise dominion over the tips (at least so far as the FLSA is concerned), and what it does with the tips from that point forward is merely a matter of what line item or bucket it chooses to allocate the tips towards, if anything in particular. The same principles that prohibit the Agency from restricting a tip pool that does not involve the tip credit necessarily prohibit the Agency from restricting the employer from exercising dominion over the tips, whether to pay the wages of the employee (or any other tipped, non-tipped, management, or non-management employee) or simply to retain them for some other general or specific purpose.

VI. THE TIP CREDIT PROVISION STILL HAS MEANING

Given that the statutory test of 3(m) provides no support for the regulation of tip retention, redistribution, etc. where the employee is not taking the tip credit for the particular tipped employee from whom the tips are taken, we recognize that those opposing USDOL's proposed action question the meaning of 3(m). While that is not the relevant question today, and again is better proposed to Congress, the idea that USDOL's proposed action renders 3(m) meaningless is easily refuted. Indeed, we expect that some employers, even knowing that the FLSA would allow them to take all of the tips, still would opt to use the tip credit in accordance with 3(m).

An employer has a vested interest in its employees providing service at or above a certain level to drive business, and in many situations patrons determine whether and to what extent to leave a tip based on a combination of the billed amount and the quality of the experience (service, product, etc.). If the employer pays 100% of the minimum wage as a cash wage and collects most or all of the employee's tips, the employee is unlikely to be as vested in providing the best service compared to when the employee retains most or all of the tips. The tip credit structure benefits both tipped employees and employers, such that both stand to gain from superior service and corresponding tips in a way that is unparalleled by a tip structure that does not implicate 3(m).

Further, at its essence, the tip credit encourages employees and employers to attempt to reach an employee's highest earning potential, while capping the employer's "risk" at minimum wage. Typically in a tipped profession, the worker is relying upon their own skills and abilities to try to maximize their tipped income. An employer who hires an inexperienced server takes a significant risk that this individual will not immediately (or perhaps ever) be able to earn sufficient tips to justify their wages. If the employee receives sufficient tips, the employer owes only the statutory direct cash wage amount (under the FLSA, $2.13 per hour). Meanwhile, the employee receives the substantial benefit of earning well more than minimum wage. On the other hand, if the employee performs poorly or takes several months to become a successful server, the employer's risk is capped at the minimum wage. Of course, if a tipped industry instead operated like others and did not have this credit available, the logical result is for employers to ban tipping, raise prices, and pay staff by the hour. To the extent that it is even relevant what an employee makes beyond the minimum wage, forgoing the tip credit reduces the opportunity for good employees to be paid virtually unlimited tipped income, but also possibly reduces the employee's incentive to provide superior service. Nonetheless, under the statutory language employers have this option. If there is opposition to that language, those efforts should be directed at Congress.

VII. CONCLUSION

Much has been made about what will occur if the USDOL's proposed changes go forward. Notably, we do not know the extent to which employers forgoing the tip credit would do any one of the following: allow employees to retain 100% of their tips still; institute tip pools that nonetheless follow the 3(m) restrictions; expand the tip pool only to include non-tipped, non-management employees (an on-going frustration in the hospitality industry); expand the tip pool to include management employees that otherwise meet the definition of a "tipped employee" based on their customer-facing positions; and/or collect and retain some or all tips for the business. Some opposing the proposed change focus almost exclusively on this last possibility, but it is just one of many. Indeed, based on our experience with the hospitality industry, the primary interest in an unrestricted tip pool is to include and recognize all members of the team of employees who are responsible for the guest experience, irrespective of any potential savings on labor costs. In the end though, the statutory text simply doesn't permit the USDOL to regulate tips outside of a tip credit arrangement. In the current context, any data on these points or in response to the questions set forth in the NPRM are irrelevant. *See* 82 Fed. Reg. 57405-6 (inquiries as to various tip practices for consideration in the NPRM analysis).

Congress made the legislative judgment that tips would not be subject to the FLSA except in limited circumstances. Congress did not address tips generally in the plain language of the statute itself (which it certainly could have done), and indeed, left no ambiguity in this regard calling for a review of legislative history. To the extent that authorities following the 1974 Amendment have inferred that the FLSA restricts tips in any other setting, their reliance on select legislative history, and subsequent reiterations, was misplaced. Instead, the USDOL's *only* authority and *sole* responsibility is to regulate tips when an employer is claiming a tip credit. The fairness of this state of affairs with respect to tips not subject to the FLSA is a fundamentally different matter of legislative policymaking to be addressed, if at all, by *Congress*.