

Has Your Tip Pool Encountered Cross Contamination?

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The recent uptick in collective action filings against Arizona restaurants compels a Human Resources focus on the requirements of tip pooling and an employer's decision to take the tip credit. With minimum wage reaching \$15.00 per hour in some cities and states, restaurateurs have been forced to address the disparity in pay rates between servers who can accept tips and kitchen staff who cannot. Many restaurants have tried to narrow the pay gap and recognize the service that kitchen staff provides to customers by instituting tip pooling policies. But restaurateurs should take care that this practice runs afoul of the Fair Labor Standards Act ("FLSA") regardless of whether a tip credit to the minimum wage is taken.

Recap on tip credit

The FLSA requires covered employers to pay employees no less than the federal minimum wage, which is currently \$7.25 per hour (\$10 per hour under the Arizona Minimum Wage Act). Under the FLSA, employers are permitted to pay tipped employees less than the minimum wage (Arizona employers taking the tip credit must pay employees \$7 per hour, \$3.00 per hour less than the Arizona minimum wage) and take a "tip credit" if the employees' tips suffice to fulfill the applicable minimum wage for the workweek. Prior to taking the tip credit, an employer must inform the employee of the FLSA's tip credit provisions.

The FLSA outlines very specific notice requirements for employers to follow. To take the tip credit, the employer must inform the employee:

1. the amount of cash wage the employer is paying the tipped employee;
2. the amount claimed by the employer as the tip credit;
3. that the tip credit cannot exceed the amount of tips actually received;
4. that all tips are to be retained by the employee (subject to a valid tip pool); and
5. that the tip credit will not apply to any tipped employee who has not received this notice.

While this notice may be oral or written, providing written notice, receipt of which is acknowledged by the tipped employee is a best practice that should be followed.

Tips belong to employees

Under the FLSA, all tips received by the employee must be retained by the employee regardless of whether the employer utilizes the tip credit. The FLSA prohibits any arrangement between the



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employer and the tipped employee that results in any part of the tip received becoming property of the employer.

This requirement does not, however, preclude a valid tip pooling arrangement. Prior to utilizing a tip pooling arrangement, the employer must notify tipped employees of any required tip pool contribution amount. Moreover, the tip pooling exception only allows “the pooling of tips among employees who customarily and regularly receive tips” (e.g., servers, bussers, bartenders, bellhops, counter personnel (who serve customers), and service bartenders). The FLSA expressly excludes dishwashers, cooks, chefs (except sushi chefs), and janitors from tip pooling arrangements. An invalid tip pooling policy will open an employer up to liability for unpaid wages.

How can companies be proactive?

Prior to taking the tip credit or implementing a tip pooling arrangement, restaurants should implement (i.e. post and distribute) a comprehensive written tip notice and pooling policy. Employers should have employees provide written acknowledgement of the receipt and understanding of the tip notice and pooling policy, and place a copy of the acknowledgement in the employee’s personnel file.

Employers using tip credits and tip pooling should regularly audit their payroll practices to ensure tipped employees are paid properly under both federal and state law. This means that employers should have a system in place to (1) ensure that an employee never falls below the minimum wage after being paid the combined hourly wage and receiving tips in any given workweek; (2) ensure that no one who is not a proper “tipped” employee is participating in a tip pooling arrangement; and (3) ensure that only actual tips received by the tipped employee is greater than the tip credit. Should the company discover non-compliance in an internal audit, it should engage counsel to determine corrective action going forward.

Clearly, these steps don’t address the pay disparity between servers and kitchen staff. If pay disparity remains a concern, consider adding a tip line on the receipt for kitchen staff. Restaurants may also eliminate tipping altogether and implement a service charge. A service charge does not constitute wages and could be divided among servers and kitchen staff at the restaurant’s discretion. But keep in mind that implementing a service charge in lieu of tips would mean not being able to take the tip credit. These ideas are being implemented in other states with success when implemented properly.