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Managing Tipped Employees:
The Implications of the \$105 Million
Starbucks Verdict

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Agenda

- Tip pooling definitions and terms
- How to ensure compliance with the FLSA
- The facts of the *Starbucks* case
- Other relevant state laws
- Best practices

Background Information

- Questions traditional practices in industries in which employees receive and share tips
- State level: more than 30 states have enacted some form of “tip” law
- Federal level: employers should also be aware of issues affecting tipped employees under the FLSA

Industries at Risk

- Any employer that relies upon “tipped employees”
 - Restaurants
 - Hotels and resorts
 - Travel
 - Beauty salons
 - Airlines
 - Casinos

FLSA Overview – Minimum Wage

- The FLSA provides that as a general rule all employees should receive at least minimum wage for all hours worked, and one and one-half times the employee's regular rate for all hours worked over 40 in a workweek.
 - The minimum wage is \$5.85 per hour, but goes up to \$6.55 on July 24, 2008, and \$7.25 on July 24, 2009.

What Is a Tip Credit?

- Section 203(m) of the FLSA allows employers to pay less than minimum wage to employees who receive tips through the use of a “tip credit”
- The “tip credit” allows employers to meet their minimum wage obligations by having a certain amount of tips count toward the minimum amount
 - Employers must pay a subminimum of at least \$2.13 per hour.

What Is a “Tipped Employee”?

- The tip credit can only be used to satisfy the minimum wage obligations for “tipped employees.” Section 203(t) of the FLSA defines a “tipped employee” as any employee engaged in an occupation in which he customarily and regularly receives \$30 a month in tips.

What Is a Tipped Employee? (cont.)

- The \$30-a-month requirement may be satisfied by receipt of tips through a tip pool.
- Occupations that typically meet the definition of a “tipped employee” include wait staff, bellhops, counter personnel who serve customers, busboys/girls, and service bartenders.
- Occupations that typically do not meet this definition include janitors, dishwashers, chefs or cooks, and laundry room attendants.
- Dual jobs
 - Duties that exceed 20%

What Is a Tipped Employee? (cont.)

- Courts will look to both quantity and quality of interaction with customers
 - Must be more than *de minimis* contact
- Must be type of work that would likely be subject to tipping
 - Simply handling customer complaints may not qualify

What Is a “Tip”?

- The regulations define a “tip” as:
 - A sum presented by a customer as a gift or gratuity in recognition of some service performed for him. It is to be distinguished from payment of a charge, if any, made for the service. Whether a tip is to be given, and its amounts are matters determined solely by the customer, and generally he has the right to determine who shall be the recipient of his gratuity. In the absence of an agreement to the contrary between the recipient and a third party, a tip becomes the property of the person in recognition of whose services it is presented by the customer. 29 C.F.R. § 531.52

How to Satisfy Minimum Wage Obligations

- To make use of a tip credit to satisfy minimum wage obligations toward an employee, the following requirements must be satisfied:
 - The employee must be in an occupation in which the employee customarily and regularly receives \$30 a month in tips
 - An employer must inform the employee of the tip credit allowance, including the amount to be credited, before utilizing the tip credit
 - Employees must be allowed to retain all tips that they receive, except in instances where pooling of tips is apportioned among other employees who customarily and regularly receive tips

What Constitutes a Valid Tip Pool?

- Can be mandated by the employer or purely voluntary
- Management personnel may not participate in tip pool
- An employer may not mandate that employees participate who are in an occupation that does not customarily and regularly receive \$30 a month in tips
- DOL takes the position that if mandated by the employer, the contributions may not exceed 15% of tips (considered “customary and reasonable”), but courts have disagreed

What Is Considered a Voluntary Tip Pool?

- Promoting peer pressure to encourage tip pooling may not be viewed as “voluntary” according to DOL

Who Is the “Employer”?

- Ownership in establishment
- Authority to hire and fire and other duties associated with “executive employees”
- Authority to send employees home and handle complaints

How to Calculate the Tip Credit and Ensure Minimum Wage Obligations Are Met

- May not count tips beyond tip credit toward minimum wage obligations
- Deductions for the employer's benefit, such as cleaning of uniforms, may not be taken against tips or subminimum wage paid
- Tips put on credit cards may be subject to service charges imposed by the credit card company, but no further deductions may be taken
- Other issues related to credit card payments

How to Calculate Overtime

- Must be based on all wages paid plus tip credit
- Do not forget to include tip credit
- Regular rate need not include tips in excess of tip credit amount
- Must include meal allowances

Potential Damages

- Difference in employee's wages to meet minimum wage if tip credit not legitimate
- In some cases, employees also may be entitled to tips taken away by employer
- Overtime liability when regular rate improperly calculated
- Liquidated damages

State Law Issues

- Is a tip credit against state minimum wage permitted?
- May the employer collect any portion of a gratuity?
- To what extent is tip pooling permitted?
- Service fee issues
 - Under what circumstances do service fees constitute gratuities?
 - Does payment of service fees to service providers count toward minimum wage?
- When must the employer pay gratuities?

State Minimum Wage Issues

- Can the employer use any portion of tips as a credit toward state minimum wage obligations?
 - Examples of states that do not permit any credit include Alaska, California, Montana, Nevada, Oregon, and Washington
- If a tip credit is allowed, how much is allowed and under what circumstances?
- What are the state's recordkeeping requirements?

State Laws Prohibiting Employer Receipt of Gratuities

- State law may differ significantly from the FLSA
- Many states specifically prohibit employers (and their agents) from collecting any portion of gratuities
- Most states allow pooling with nonemployers who service customers
- Who constitutes an employer and/or an agent of an employer may vary from state to state

State Laws on Tip Pooling

- Two sources of prohibitions on tip pooling
 - Tip credit against state minimum wage laws
 - Prohibitions on collecting gratuities
- Generally limited to employees who interact with customers
- Often, employers and/or agents cannot receive any portion of the pool
- Remedy (state specific)
 - Recovery of “pooled” amount
 - Recovery of minimum wage
 - Penalties

State Laws Regarding Service Fees

- State laws vary significantly with respect to “service fees”
 - Nonvoluntary payments of specific amounts
 - Bag check fees, valet fees, room service fees, banquet fees, etc.
- Does payment of service fees count toward minimum wage?
- Do laws prohibiting tip pooling apply to service fees?
- Do laws prohibiting collection of gratuities apply to service fees?
- Several states (e.g., MA, NY) evaluate whether the patron has a reasonable expectation that the “fee” will be paid to the service provider

California Example

- No employer or agent shall collect, take, or receive any gratuity or part thereof that is paid, given to, or left for an employee by a patron, or deduct any amount from wages due an employee on account of a gratuity, or require an employee to credit the amount ... of a gratuity against and as a part of the wages due the employee from the employer. Every gratuity is hereby declared to be the sole property of the employee . . . to whom it was paid, given or left for. An employer that permits patrons to pay gratuities by credit card shall pay the employees the full amount of the gratuity that the patron indicated on the credit card slip, without any deductions for any credit card payment processing fees or costs that may be charged to the employer by the credit card company. Payment of gratuities made by patrons using credit cards shall be made to the employees not later than the next regular payday following the date the patron authorized the credit card payment.

Chau v. Starbucks Corp.
Case No. GIC836925

- Baristas and shift supervisors shared responsibility for making drinks, serving customers, and working cash register
- Patrons contributed money to tip jars located at cash register
- Tips were distributed among baristas and shift supervisors
- Shift supervisors are hourly employees

Chau v. Starbucks Corp. (cont.)

- The plaintiffs argued that Starbucks's tip-pooling policy was illegal
 - Shift supervisors were “agents” of the employer and not entitled to a share of the tips
 - Statute defines “agent” as “every person other than the employer having the authority to hire or discharge any employee or supervise, direct or control the acts of employees.”
- Judgment: \$86 million in restitution; \$19 million in interest
- New York, Minnesota, and Massachusetts suits followed

DiFiore v. American Airlines, Inc. (Mass.)

- Under Mass. law service charges are treated as tips where the patron would reasonably expect the fee to be given to the service provider in lieu of, or in addition to, a tip
- Mass. law prohibits employers from collecting any portion of tips
- American instituted a \$2-per-bag service charge for skycaps
- Skycaps argued that American failed to adequately notify patrons that the service charge was not a tip

Best Practices

- Investigate applicable state law
- Be sure to comply with all applicable minimum wage laws
- Carefully evaluate applicable law where tip pools include anyone with a supervisory role
- Limit tip pools to employees who interact significantly with patrons
- Clearly disclose that service fees are not tips (if appropriate)

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