

Restaurants and those in the Hospitality Business should not rely on a faulty or simply wrong understandings of wage & hour laws. Mistakes can be very painful. By Gary S. Young, Partner, Mandelbaum Barrett P.C.

Employers of tipped employees in the restaurant and hospitality industries know that it is common practice for such workers to share tips (tip pools). It is argued that tip pools promote teamwork and a better customer experience—but tip pooling exposes employers to significant liabilities unless federal and state wage and hour laws are followed **with precision**. We know that running a business carries many risks. When it comes to wage & hour compliance, knowing and following the law is never optional. The problem is that many industry employers “think” that they know the law when they really do not.

For example, the Department of Labor (DOL) recently found there was a significant violation of the Fair Labor Standards Act (FLSA) when a big restaurant chain allowed its hourly managers to participate in a tip pool. The restaurant chain was found to owe its employees almost \$1.0 million in unpaid tips and overtime premiums.

Most restaurant owners know that federal law (“FLSA”) permits employers to take a so-called “tip credit” and pay employees who traditionally receive tips—such as servers and bartenders—less than the federal minimum wage so long as tips make up the difference **and the employer follows all other legal requirements**. The FLSA defines a “tipped employee” as “any employee engaged in an occupation in which he customarily and regularly receives more than \$30 a month in tips.” As the first order of business, new hires should be informed whether they will be classified as tipped employees to be sure that this is understood.

New Jersey complicates compliance with the imposition of higher minimum standards. Complete compliance with all FLSA requirements may still run afoul of New Jersey law. In 2019, New Jersey scheduled annual increases to the minimum wage while limiting the amount of tip credit that the employer may take. For 2022, the minimum wage was set at \$13.00, the minimum cash wage for tipped employees at \$5.13 and the maximum tip credit at \$7.87. These amounts will increase in 2023 to \$14.00, \$5.13 and \$8.87 respectively.

These minimums significantly differ from federal law. While federal law will always set the minimums for these issues (assuming that your business’s activities are in the flow of interstate commerce), the states like New Jersey can always set higher minimum standards.

Here are some of the trouble spots where employers must pay particular attention:

- First, inform your employees if you are classifying them as being “Tipped Employees”; in such case, all of the rules must be applied properly with no leeway for mistakes;
- Tip pools are permissible; but if you violate the rules, you will destroy the tipped employee’s classification (as was the chain restaurant case cited above);
- Management employees cannot share tips with tipped employees;
- Generally, back of the house employees cannot share in tips; there is an exception under federal law: if you pay the tipped employees the full minimum wage (\$14.00 in 2023)

and further provided that no tip credit is taken by the employer, tips can be shared with back of the house employees; caution: this still may not be accepted by New Jersey;

- Employers can never take any portion of tips paid to employees under any circumstance as tips are the property of the employees exclusively; but “service charges,” which are not tips, can be applied by employers much differently (the rules vary from state to state);
- Overtime for tipped employees is a complicated area; many employers make significant mistakes in paying overtime to tipped employees;
- Care must be given where the tipped employee spends more than 20% of work time performing non-tipped work; similar complications arise when an employee mixes activities from tipped work to non-tipped work in a work week; under a final rule from the Biden administration, an employer loses the tip credit if a tipped employee spends more than 20 percent of their weekly hours performing work that is not tip-producing work or work that directly supports tip-producing work. The final rule, which took effect in December 2021, also requires employers to pay tipped employees the full minimum wage when they spend at least 30 continuous minutes on secondary duties that don't generate gratuities; and
- Where an employee works in more than one restaurant owned by the same or similar owners (defined as being a “controlled group” in the Internal Revenue Code), care must be given to wage compliance and calculations of overtime.

While federal and state law are frequently similar, differences have increased where New Jersey which has opted to exercise its right to regulate the wages of hospitality workers that diverges from federal law. A good example involves the deduction of credit card fees. Federal law permits the employer to deduct the credit card fee attributable to the tip, for many years, New Jersey agreed but now no longer permits this. If you have been doing this for a long time, you may not have noticed that the New Jersey changed the law (years ago).

Besides the obvious factor of how complicated and challenging the law and compliance is, the restaurant and hospitality industries are increasingly exposed to legislative divergence. This is not an area where amateurs thrive. You need to know the law and apply it properly or pay the consequence! Call us for help.