

FAQs on Compliance With the Federal Tip Credit

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What is the tip credit and how much is it worth?

Under the FLSA, employers are required to pay non-exempt employees the applicable federal minimum wage, which is currently \$7.25 per hour. If the criteria set forth below are met, an employer may pay an employee as little as \$2.13 per hour in “cash wages,” with the tip credit making up the remaining \$5.12 per hour to meet the minimum wage. The tip credit may only be utilized with those employees who meet the FLSA's definition of a “tipped employee.”

Do state tip credit laws differ from the federal law?

Many states have higher minimum wage requirements than the FLSA and/or have different rules regarding the applicability of and the criteria for utilizing a tip credit. Employers should ensure that their wage and tip payment practices comply both with the FLSA and applicable state law.

Who qualifies as a “tipped employee?”

Under the FLSA, a tipped employee is an employee who customarily and regularly receives more than \$30 per month in tips. Positions that typically qualify as tipped employee positions include servers, bartenders,

buspersons, and valets. Employees who may occasionally receive tips but who do not receive such tips on a regular basis and do not meet the \$30 per month threshold are not considered tipped employees.

What steps does an employer have to take to implement the tip credit for tipped employees?

First, an employer must give notice to the tipped employee that the employer is going to utilize the tip credit. This notice does not need to be in writing, but it is highly recommend that employers put the notice in writing so that the employer has evidence that the notice was, in fact, given. Better yet, employers should have tipped employees sign an acknowledgment that they have received the notice. The notice must include the following information:

- the amount of cash wage the employer will be paying the tipped employee (which, by law, should be a minimum of \$2.13 per hour);
- the amount the employer will be claiming as the tip credit (which, by law, may not exceed a maximum of \$5.12 per hour);
- the claimed tip credit cannot exceed the amount of tips received by the tipped employee;
- all tips received by the tipped employee will be retained by the employee except in situations in which the employer has established a valid tip pool; and
- the tip credit will not apply to any employee unless the employee has been provided with this notice.

Second, the employer must allow the tipped employee to retain all tips received, except in situations in which the employer has established a valid tip pool, which is explained below.

Third, the employer must ensure that the tipped employee earns at least enough tips in a workweek to equal the amount of the tip credit being taken. For example, if the employer is taking a tip credit of \$5.02 per hour, the employer must ensure that the employee has received tips during the workweek to equal at least \$5.02 per hour for the hours the employee worked that week. The employer should require all tipped employees to report 100 percent of their tips and should retain accurate records of this reporting as evidence that the employees earned sufficient tips to support the tip credit.

Can the employer keep any portion of the tips or require a tipped employee to share tips with another employee?

As the notice above states, in order to qualify as a tipped employee for purposes of the tip credit, the employee must retain all tips received, apart from those contributed to a valid tip pool. An employer may not require a tipped employee to pay to the employer, or anyone else not part of a valid tip pool, any portion of their tips. However, where a tip is paid on a credit card and the credit card company charges the employer a transaction fee based on a percentage of the amount of the charge, the employer may deduct that same percentage from the employee's tip. For example, if the transaction fee is 2 percent and the employee

received a \$10.00 tip on a credit card, the employer could deduct 20 cents from the amount to be paid to the employee.

What constitutes a valid tip pool?

A valid tip pool is one in which tips are shared between and among a group of employees who customarily and regularly receive tips. For example, a group of restaurant servers can pool together a portion of their tips to share with the bartender and busperson who assisted them. A tip pool that includes individuals who do not customarily and regularly receive tips—such as managers, janitors, and cooks (although there may be some exceptions)—is not valid and may negate the tip credit.

What happens if an employer utilizes the tip credit without giving employees the required notice?

An employer that fails to provide proper notice of the tip credit is not entitled to take the tip credit and must pay its employees the minimum wage of \$7.25 per hour. Where an employer is found to have taken the tip credit without giving the proper notice, the employer may be required to pay the difference between the cash wage and the minimum wage for the period of time before the employer provided notice.

What happens if, in a given week, the tipped employee does not earn enough tips to equal the amount of the tip credit taken?

If an employee does not earn sufficient tips to equal the tip credit in a given week, the employer is required to pay the employee an amount needed to make up the difference. For example, if the employee worked 30 hours in the workweek, received \$2.13 per hour in cash wages and received \$100.00 in tips during the week, the employer would be required to pay the employee an additional \$53.60 in cash wages to make up the difference between the tips received and the tip credit amount.

How does an employer calculate overtime for a tipped employee?

To determine the cash wage to be paid to a tipped employee for purposes of overtime compensation, the employer must calculate the overtime rate based on the full minimum wage, subtract the amount of the tip credit, then pay the rest in a cash wage. The amount of the tip credit the employer takes will affect the amount of cash wages to be paid for the overtime hours worked. Here are some examples:

- Example A: The employee receives a cash wage of \$2.13 per hour and the employer takes a tip credit of \$5.12 per hour. The employee's total minimum wage is \$7.25 per hour. The overtime rate is \$10.88. The overtime cash wage is \$5.76 per hour.
- Example B: The employee receives a cash wage of \$3.00 per hour and the employer takes a tip credit of \$4.25 per hour. The employee's total minimum wage is \$7.25 per hour. The overtime rate is \$10.88. The overtime cash wage is \$6.63.

If an employee makes more tips than would be necessary to equal the tip credit, can the employer retain some of that money or take deductions from the employee's wages for work-related items such as uniforms?

Where the employer is utilizing the tip credit, the tipped employee is treated as making the minimum wage no matter how much the employee earns in tips (as long as the employee earns enough tips to equal the tip credit amount). The employer's retention of tips outside of a valid tip pool would render the tip credit invalid. In addition, if an employer makes any deductions for work-related items, they would be considered deductions that drop the employee below the minimum wage. This is true even where the employee earns hundreds of dollars per week in tips, bringing his or her actual hourly rate well above the minimum wage.

If a tipped employee performs some tasks that are not directly related to serving the customers who pay tips, does that affect how the employer must pay the employee?

Many tipped employees' jobs may require the employee to perform some number of tasks that are not directly related to serving the customer. For example, a server may also fold napkins or perform other restaurant work and a bartender may cut lemons and prepare the bar area in addition to serving customers. As long as these types of tasks do not exceed 20 percent of the employee's work time during the workweek, they do not have any effect on the employee's compensation. However, where the employee is essentially working in two different positions—e.g., working some shifts as a server and others as a cook—the employer may only utilize the tip credit for those hours the employee spends performing the tipped work.

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