

Federal Court Strikes Down Tip Credit Rule Promulgated by the DOL

AUGUST 29, 2024

Authors: [W. Eric Baisden](#), [Adam Primm](#), [Hannah J. Kraus](#)

On August 23, 2024, the Fifth Circuit Court of Appeals struck down a final rule promulgated by the Department of Labor (“DOL”) restricting when employers could take a tip credit for tipped employees under the Fair Labor Standards Act (“FLSA”). This decision comes in the wake of the Supreme Court’s landmark decisions in *Loper Bright and Relentless*, which overturned the highly deferential standard for judicial review of agency regulations set forth in *Chevron v. Natural Resources Defense Council*.

Tip Credits Under the FLSA

Under the FLSA, employers are permitted to take a tip credit towards minimum wage obligations when paying the wages of a tipped employee. A “tipped employee” is defined as “any employee engaged in an occupation in which he customarily and regularly receives more than \$30 a month in tips.” Employers are permitted to pay tipped employees at a rate of \$2.13 per hour, which is significantly less than the current federal minimum wage of \$7.25 per hour, because a substantial portion of tipped employees’ earnings come from tips. A tipped employee’s hourly rate and tips, when combined, must be equal to or exceed the minimum wage. The FLSA requires employers to pay the difference if the hourly rate and tips do not meet or exceed the minimum wage for the hours worked.

The DOL’s 80/20/30 Rule

The rule at issue in this case sought to put certain parameters on when employees could be treated as tipped employees to legally receive a tipped wage. Historically, the DOL had authority to promulgate rules interpreting the FLSA, and the tip credit has been the subject of interpretation for decades. The DOL’s most recent interpretation of tip credits became effective in December 2021 and is widely known as the “80/20/30 Rule.” Under the 80/20/30 Rule, the DOL defines three distinct categories of work: (1) directly tip-producing work; (2) directly supporting work; and (3) work not part of the tipped occupation.

Employers can take tip credits for any “directly tip-producing work,” which is any work for which employees receive tips (i.e., a server serving customers). On the other hand, employers cannot take tip credits for any “work not part of the tipped occupation” (i.e., a server preparing food). The definition of “directly supporting work” (i.e., a server setting and bussing tables) is more ambiguous and fluid. Under the 80/20/30 Rule, employers could not take tip credits for any “directly supporting work” that exceeds 20% of a tipped employee’s total hours for the workweek or that is performed for more than 30 continuous minutes.

The Fifth Circuit's Decision

Shortly after the 80/20/30 Rule took effect, the Restaurant Law Center and the Texas Restaurant Association filed a lawsuit in the Western District of Texas to enjoin the DOL's enforcement of the 80/20/30 Rule. The plaintiffs argued that the 80/20/30 Rule was contrary to the text of the FLSA and arbitrary and capricious under the Administrative Procedures Act ("APA"). The District Court upheld the 80/20/30 Rule, concluding that the DOL's interpretation of tip credits was entitled to deference under the *Chevron* doctrine.

On appeal, the Fifth Circuit reversed the District Court and struck down the 80/20/30 Rule. In light of *Chevron* being overturned by *Loper Bright* and *Relentless* during this case, the Fifth Circuit ignored the *Chevron* standard and instead returned to traditional statutory interpretation. The Fifth Circuit ultimately determined that the 80/20/30 Rule "applies the tip credit in a manner inconsistent with the FLSA's text." Specifically, the Fifth Circuit emphasized that the FLSA is not concerned with whether each specific duty of a tipped employee is necessarily tip-producing. Rather, the FLSA allows tip credits for any employee "engaged in an occupation...that customarily and regularly receives more than \$30 a month in tips" regardless of whether each specific duty of the occupation is tip-producing. The Fifth Circuit further concluded that the 80/20/30 Rule "is arbitrary and capricious because it draws a line for application of the tip credit based on impermissible considerations to the statutory scheme enacted by Congress."

Implications of This Decision

The Fifth Circuit's decision is a major win for employers, especially those in the restaurant and hospitality industry. Following the Northern District of Texas's recent decision to vacate the Federal Trade Commission's ban on non-compete agreements, this decision continues to demonstrate the significant impact that the *Loper Bright* and *Relentless* decisions already have and will continue to have on federal labor and employment regulations moving forward. Now that agencies are not supported by, and cannot rely upon, broad deference under *Chevron*, we will continue to monitor and report on future agency regulations that will inevitably be impacted by the overturning of *Chevron*.

For more information, contact a member of Benesch's Labor & Employment Practice Group.

W. Eric Baisden at ebaisden@beneschlaw.com or 216.363.4676.

Adam Primm at aprimm@beneschlaw.com or 216.363.4451.

Hannah J. Kraus at hkraus@beneschlaw.com or 216.363.6109.