



January 13, 2006

FLSA2006-1

Dear *Name** :

This is in response to your request for an Administrator's opinion letter regarding the application of the Fair Labor Standards Act (FLSA) to deductions from tips earned by servers employed by your client. The tips in question are those that restaurant patrons have added to the credit card payment of their food and beverage bills. It is our opinion that, although employers may deduct an average standard composite amount from tip transactions in some circumstances, rather than the exact charges associated with each individual transaction, in the aggregate the employer may recapture no more than the total charges imposed by credit card companies attributable to liquidating credit card tips.

You have provided a detailed four-page breakdown of the costs you believe result from liquidating charged tips to cash during the period September 1999 to September 2001. In addition to the average credit card fee of 2.9%, you included other expenses that brought the employer's total cost to 4.8%. The additional costs that you added include the "time value of credit card collections" (which included "internal time processing credit cards charges" and "internal time reconciling credit card charges"), credit card charges for gift certificate sales, the cost of the credit card terminal and dedicated phone lines, "house account collections," and "house account charge and collection costs." (The difference between the last two costs was not clear.)

You quote the court in *Myers v. Copper Cellar Corp.*, 192 F.3d 546, 554 (6th Cir. 1999), which held that an employer "has an obvious legal right to deduct the cost of converting the credited tip to cash." You interpret the court's decision as further recognizing that standard composite percentage deductions may exceed specified credit card fees by including other costs incurred indirectly by the employer, including losses and interest during the settlement period.

You asked the following question:

May our client, a restaurant-employer take an average standard composite percentage deduction from its server's tips to cover the cost of liquidating charged tips? And, if so, what specified direct costs in addition to credit card fees may it include in computing the standard composite percentage deduction?

Section 3(m) of the FLSA (copy enclosed) provides that "[i]n determining the wage an employer is required to pay a tipped employee, the amount paid such employee by the employee's employer shall be an amount equal to—1) the cash wages paid such employee which for purposes of such determination shall be not less than the cash wage required to be paid such an employee on August 20, 1996; and 2) an additional amount on account of the tips received by such employee which amount is equal to the difference between the wage specified in paragraph (1) and the wage in effect under section 206(a)(1) of this title. The additional amount on account of tips may not exceed the value of the tips actually received by an employee. The preceding 2 sentences shall not apply with respect to any tipped employee unless such employee has been informed by the employer of the provisions of this subsection, and all tips received by such employee have been retained by the employee, except that this subsection shall not be construed to prohibit the pooling of tips among employees who customarily and regularly receive tips." 29 U.S.C. § 203(m).

We do not read the Sixth Circuit's decision in *Copper Cellar* as broadly as you suggest. That decision recognized that different credit card companies charge merchants slightly different percentage processing fees. In that case, rather than deducting from employees' tips the precise service charge each credit card company assessed, the employer deducted a standard fixed amount of 3%, which "sometimes slightly exceeded, but on other occasions fell short of, the



financial institution's actual processing fee levied for the subject charged tip." See *Copper Cellar*, 192 F.3d at 553. The employer in that case also "absorbed all losses" caused by the charges that were uncollectible and did not charge employees interest on the use of the funds it advanced before the charges cleared. *Id.* at 553 n.13. The court approved the "standard composite percentage" only in circumstances where the employer demonstrates "that, *in the aggregate*, the amounts collected from its employees, over a definable time period, have reasonably reimbursed it for no more than its *total expenditures associated with credit card tip collections*." *Id.* at 554 (second emphasis added). Such deductions, the court concluded, must not enrich the employer, "but instead, at most, merely restore[] it to the approximate financial posture it would have occupied if it had not undertaken to collect credit card tips for its employees." *Id.* at 555. Moreover, the court referred with approval to the Wage and Hour Division's position, described below, permitting an employer to subtract only "the tip collection fee from the employee's gratuity." *Id.* at 554.

Where tips are charged on a credit card, it is the position of the Wage and Hour Division that the tips due the employee must be paid to the employee not later than the next regular pay day and may not be held by the employer while the employer is waiting to be reimbursed by the credit card company. See Field Operations Handbook (FOH) ¶ 30d05(b) (copy enclosed). However, where a credit card charge is uncollectible, the Wage and Hour Division does not require an employer to pay an employee the amount of tips specified on such credit card slips. Instead, the employer may recover from a tipped employee those tips that have been paid to the employee when the credit card charge is uncollectible; however, such recovered tips may not reduce the tips retained by the employee below the amount of the tip credit claimed. See FOH ¶ 30d05(c)-(d).

Furthermore, the Wage and Hour Division does not question the practice whereby the employer reduces the amount of credit card tips paid to the employee by an amount no greater than the amount charged to the employer by the credit card company. See FOH ¶ 30d05(a). The employer's deduction from tips for the cost imposed by the credit card company reflects a charge by an entity outside the relationship of employer and tipped employee. However, it is the Wage and Hour Division's position that the other costs that your client wishes the tipped employees to bear must be considered the normal administrative costs of your client's restaurant operations. For example, time spent by servers processing credit card sales represents an activity that generates revenue *for the restaurant*, not an activity primarily associated with collecting tips. Likewise, the time spent in other activities you mention represents merely the reasonably incurred administrative costs of a restaurant that chooses to accept credit card payments. See Opinion Letters dated March 28, 1977 and February 26, 1998 (copies enclosed). Moreover, the cost of dedicated phone lines and the time spent processing the transactions are the same whether or not a tip is included on the bill. An employer may deduct an average standard composite amount for tip liquidation, rather than individually calculating the precise charge for each transaction, so long as the total amount collected reasonably reimburses the employer for no more than the total amounts charged by the credit card companies attributable to liquidating credit card tips. Any employer attempt to deduct an average standard composite amount for tip liquidation that exceeds such expenditures is not acceptable.

This opinion is based exclusively on the facts and circumstances described in your request and is given based on your representation, express or implied, that you have provided a full and fair description of all the facts and circumstances that would be pertinent to our consideration of the question presented. Existence of any other factual or historical background not contained in your letter might require a conclusion different from the one expressed herein. You have represented that this opinion is not sought by a party to pending private litigation concerning the issue addressed herein. You have also represented that this opinion is not sought in connection with an investigation or litigation between a client or firm and the Wage and Hour Division or the Department of Labor. This opinion is issued as an official ruling of the Wage and Hour Division for purposes of the Portal-to-Portal Act, 29 U.S.C. § 259. See 29 C.F.R. §§ 790.17(d), 790.19; *Hultgren v. County of Lancaster*, 913 F.2d 498, 507 (8th Cir. 1990).



We trust that the above information is responsive to your inquiry.

Sincerely,

Alfred B. Robinson, Jr.,
Deputy Administrator

Enclosures:
FLSA § 3(m)
FOH ¶30d05
Opinion Letters dated March 28, 1977 and February 26, 1998

** Note: The actual name(s) was removed to preserve privacy in accordance with 5 U.S.C. § 552 (b)(7).*