

An hourglass-shaped graphic with a globe in the top bulb and another globe in the bottom bulb. The hourglass is light blue and has a dark blue top and bottom. The globe in the top bulb is dark blue, and the globe in the bottom bulb is light blue. The text is centered within the hourglass.

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*The Tip Credit Provisions of the Fair Labor Standards Act*

William G. Whittaker, Domestic Social Policy Division

March 24, 2006

**Abstract.** This report discusses the tip system under the FLSA, its application under state standards, and the status of the related sub-minimum wage worker. Given the history of the act, it seems likely that some further discussion of these issues will take place.

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# CRS Report for Congress

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## The Tip Credit Provisions of the Fair Labor Standards Act

**March 24, 2006**

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<http://wikileaks.org/wiki/CRS-RL33348>

# The Tip Credit Provisions of the Fair Labor Standards Act

## Summary

The Fair Labor Standards Act (FLSA) is the primary federal statute dealing with wages, hours, and conditions of employment. One aspect of wage policy is the question of *tip income*. Closely related to the issue of tip income is the ability of employers, under the FLSA, to employ certain youth workers at *sub-minimum wages*.

During the 1960s, the FLSA was expanded to include certain areas of work that had been omitted from the 1938 statute. Among them were workers engaged in the service and retail trades. Since many such workers received tips in the normal course of their work (some of them, a substantial amount of tips), the question arose as to how they were to be treated in the context of a federal minimum wage structure.

There had been some discussion of the tip question prior to 1938 but, since the initial enactment really did not cover many workers in tipped occupations, it was not made a part of the act. In the 1960s, however, the issue became somewhat more controversial. Did tips flow, almost necessarily, from the ambience of the restaurant or club — the nature of a hotel or inn? If so, were tips really the product of employer contributions — and should they belong to the employer? If they should not actually become the property of the employer, should an offset be made against the minimum wage?

Workers were adamant that employment should bring *a wage* — and also that the wage was to be paid by the employer: a steady wage and a consistent wage, not just a gratuity voluntarily given by a third party. The rationale was that an employee could assist in development of a business by his or her graciousness; or, on the other hand, could contribute to a decline in business were he or she to render shoddy service or make a customer feel uncomfortable or unwelcome. From this perspective, the tip should be the property of the employee: *a gift* from the served to the server.

But what about the other employees of the establishment (those who are unseen by the customer)? Indifference in the kitchen could diminish a tip. Meanwhile, expert assistance from support staff could enhance tip income and encourage a client to return. Should some consideration be given to the invisible (but vitally important) *back-of-the-house* staff? Perhaps a *pooling of tips* might be useful?

Aside from the federal wage/hour law, there exist multiple state standards that govern tips and tip income. How are they to be meshed with the federal FLSA?

This report discusses the tip system under the FLSA, its application under state standards, and the status of the related sub-minimum wage worker. Given the history of the act, it seems likely that some further discussion of these issues will take place. As that discussion develops, the report will be revised.

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# The Tip Credit Provisions of the Fair Labor Standards Act

During the 1960s, with amendment to the Fair Labor Standards Act (FLSA), Congress included a provision for a *tip credit* under the federal minimum wage for employers of *tipped employees*. Through the years, although the tip credit has been altered, it remains a part of the act.<sup>1</sup>

Under the FLSA, a tipped employee (one who earns at least \$30 a month in tips) may have his or her federal minimum wage reduced to \$2.13 per hour (cash paid by the employer) — assuming that the combination of tips and cash income from the employer, collectively, equals the federal minimum wage (i.e., \$5.15 per hour). Thus, *all covered workers earn at least the federal minimum wage of \$5.15 per hour* — except for “sub-minimum wage” earners. For a non-tipped worker, the entire amount of the minimum wage derives from cash wages from the employer. For the tipped employee, no less than \$2.13 comes from the employer in cash, with the remainder accountable in tips, assuming that he or she actually earns a sufficient amount to equal the minimum wage. If there is a deficiency, the remainder must be made up by the employer.<sup>2</sup>

There were no employer qualifications involved in establishing the \$2.13-per-hour tip-based figure — though proponents of the tip credit assert that there is and, indeed, from their perspective, there may be. It is the employer who creates the *ambience* — the environment in which the employee works and in which the customer determines the tip. The \$2.13, some would argue, may be attributable to *ambience* (or to other similar factors).

Speaking generally, organized labor (and tipped employees) may be said to have preferred a zero tip credit. Whatever income was derived from tips, they suggest, should be the property of the tipped employee: a gratuity from the person being served to the server. Payment for employment, some argue, should come from the

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<sup>1</sup> The *tip credit*, technically, is that portion of the wage of a minimum wage employee that the employer is allowed to retain as an offset, presumably, for his or her contribution to receipt of a gratuity. Or, viewed from another perspective, it can be seen as a reduction in the minimum wage for a tipped employee. *However*, all otherwise covered employees receive the minimum wage: some, from his or her employer; others, in combination of an employer contribution and gratuities from a consumer. The process through which the tip credit is calculated can be termed the *tip credit provision* of the Fair Labor Standards Act.

<sup>2</sup> In 1996, Congress divided the then-current minimum wage (\$4.25) in half, establishing the tip credit at one-half of the minimum wage (\$2.13 per hour); and then, having locked in the tip credit provisions, Congress — in a separate action — increased the minimum wage to \$5.15 per hour. But for purposes of calculating the tip credit, the \$4.25 figure remains the base rate (i.e., \$2.13 for the employer and \$2.13 for the worker).

employer — a regular wage that is steady and reliable. Conversely, still speaking generally, industry would prefer a 100% credit. From this viewpoint, the employer provides the context for services and should be properly reimbursed; thus, whatever whatever gratuity might be received should go to the house (however defined).

## Evolution of *Tip Credit* Coverage

In 1938, after decades of debate and analysis and much experimenting with state statutes, Congress adopted the Fair Labor Standards Act. The act established a minimum wage for certain workers, set overtime pay at one and one-half times the worker's regular rate of pay and, among other things, placed restrictions upon child labor. The act has undergone general revision on eight separate occasions — with other more specific amendments as determined to be needed.

Minimum wage initiatives began with the states during the first decade of the 20<sup>th</sup> century, but were generally declared unconstitutional by the courts where they had effect. In 1937, in the Washington state case of *West Coast Hotel Co. v. Parrish*, the Supreme Court reversed its long-standing antipathy toward minimum wages, affirming the right of states to intervene in wage/hour policy. Thereafter, both the states and the federal government moved to enact laws governing minimum wages and associated patterns of employment.<sup>3</sup>

During the summer of 1938, Congress adopted the FLSA, beginning with relatively modest coverage. Initially, persons in the retail and services trades, among many others, were excluded from coverage — though some of those excluded may have been significantly disadvantaged in economic terms.<sup>4</sup> Very gradually, first one segment of the workforce and then another were given wage and hour protections under the FLSA — with the greatest coverage extensions occurring during the 1960s.

In the 1961 amendments, the Secretary of Labor was instructed to explore “the complex problems involving rates of pay of employees in hotels, motels, restaurants, and other food service enterprises who are exempted from the provisions of this Act” and to submit a report to the Congress. The result was two reports, each heavily statistical, that examined the general issue of tipped (and non-tipped) employment.

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<sup>3</sup> *West Coast Hotel, Co. v. Parrish*, 300 U.S. 379 (1936). See John W. Chambers, “The Big Switch: Justice Roberts and the Minimum-Wage Cases,” *Labor History*, winter 1969, pp. 44-73.

<sup>4</sup> See Henry R. Seager (edited by Charles A. Gulick, Jr.), *Labor and Other Economic Essays* (New York, Harper & Brothers Publishers, 1931), pp. 214-226, 386-398; and Dana Frank, “Girl Strikers Occupy Chain Store, Win Big: The Detroit Woolworth's Strike of 1937” (edited by Howard Zinn), *Three Strikes: Miners, Musicians, Sales Girls, and Fighting Spirit of Labor's Last Century* (Boston, Beacon Press, 2001), pp. 59-118. See also the comments of Representative Fred Hartley (R-NJ), *Congressional Record*, June 14, 1938, pp. 9257-9258, concerning exclusions from coverage.

Through that mechanism, the visibility of the issue was raised and the foundation was laid for subsequent actions.<sup>5</sup>

## Institution of the Tip Credit during the 1960s

During the course of several years, the tip credit provision gained momentum. “Extension of the minimum wage to hotels and motels is now a mere formality,” observed Jim Snyder, a regular columnist for *Hotel Management Review & Innkeeping*. Regarding the loss of “their 38-year-old fight,” Snyder reported:

“‘We’ve lost all right,’ philosophized one AH&MA [American Hotel and Motel Association] spokesman. ‘But when you consider that the industry has saved a million dollars or so every day it’s been exempt, I guess you could say that the effort was worthwhile.’”<sup>6</sup>

In the 1966 amendments, the new *tip credit provision* was added to the FLSA — in the face of a significant amount of opposition.

The 1966 amendments to the FLSA, however, were not a total loss to industry. First, a *tipped employee* was defined as anyone who “*customarily and regularly* receives more than \$20 dollars a month in tips.”<sup>7</sup> Second, an employer would be able to count up to 50% of the applicable minimum wage, ordinarily payable in cash to the employee, through a tip credit arrangement.<sup>8</sup> If the employee felt that he or she had been short-changed in the process, an appeal could be made to the Department of Labor showing “to the satisfaction of the Secretary that the actual amount of tips received by him was less than the amount determined by the employer” — and his wage would be increased accordingly.

Though minimum wage coverage, however modified, had been extended to the service industries (inter alia, hotels, motels, restaurants), there was another offsetting provision built into the act in 1966. Historically, the Secretary of Labor had been given the option of applying a *sub-minimum wage* (“... to the extent necessary in order to prevent curtailment of opportunities for employment...”) to persons engaged as learners, apprentices, and messengers.<sup>9</sup> Under the 1961 amendments, the

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<sup>5</sup> P.L. 87-31, Section 13. See U.S. Department of Labor, Wage and Hour and Public Contracts Divisions, *Hotels and Motels and Restaurants and Other Food Service Enterprises*, each dated February 1962, and transmitted by Arthur J. Goldberg, Secretary of Labor.

<sup>6</sup> *Hotel Management Review & Innkeeping*, Aug. 1966, p. 10. See also comments of Representative Joseph Minish (D-NJ), *Congressional Record*, May 24, 1966, p. 11298.

<sup>7</sup> P.L. 89-601, Section 101. Italics added. With each series of amendments after 1966, changes were made in the precise terms of the tip credit provisions. See discussion below.

<sup>8</sup> Again, where there were insufficient tips to cover the 50% credit, the employer would need to assume responsibility for payment to the employee.

<sup>9</sup> P.L. 75-718, Sections 13 and 14. Since the *sub-minimum wage* and the *tip credit* (continued...)

provision had been amended by adding “full-time students outside of their school hours” insofar as “such employment is not of the type ordinarily given to a full-time employee.”<sup>10</sup>

With the 1966 amendments, the student sub-minimum was expanded with a wage “not less than 85 per centum of the minimum wage,” then applicable to other covered workers, to apply to such student workers.<sup>11</sup> The provision, it was affirmed, would have exempted child labor but would, at the same time, have opened the field to college or other students in professional fields — who could, ordinarily, have been employable but who, now, might be employable at a sub-minimum rate. A further subsection was added to permit such employment in agriculture.

## The 1974 Amendments

Adjustment of the tip credit provision was largely technical in the 1974 amendments. The credit remained at 50%. Use of the tip credit by the employer, it appeared, came to rest upon the premise that all tips would be retained by the employee. In addition, there was added a provision for the pooling of tips: “... this subsection shall not be construed to prohibit the pooling of tips among employees who customarily and regularly receive tips.”<sup>12</sup>

## The 1977 Amendments

The tip program was restructured under the 1977 FLSA amendments. The threshold for instituting a tip credit was moved from \$20 per month to \$30 per month. While one could argue that the dollar amount was being raised in keeping with inflationary pressures, it might also be pointed out that the Congress diminished

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<sup>9</sup> (...continued)

provisions of the FLSA apply, often, to the same industries and personnel as an offset to the standard minimum wage, a brief explanation of the evolution of the sub-minimum wage is presented here.

<sup>10</sup> P.L. 87-30, Section 11. The provision may have been difficult to enforce in that it would seem nearly impossible, given enforcement/compliance staff requirements, to ascertain which jobs would not have been, ordinarily, offered “to a full-time employee.” The student sub-minimum rate at 85% of the otherwise standard minimum, subject to statutory requirement, remains a part of the act.

<sup>11</sup> P.L. 89-601, Section 501.

<sup>12</sup> P.L. 93-259, Section 13. *Tip pooling* is the practice of sharing tips with non-service personnel (for example, the kitchen help) who contribute to the service that makes tips more likely. The 1974 amendments also provide that an institution of higher education, attended by the student, may employ full-time students on a part-time basis at a sub-minimum wage.

U.S. Department of Labor, Employment Standards Administration, Wage and Hour Division, *Fact Sheet No. 15: Tipped Employees Under the Fair Labor Standards Act (FLSA)*, Mar. 1, 2006, notes: “The law forbids any arrangement between the employer and the tipped employee whereby any part of the tip received becomes the property of the employer. A tip is the sole property of the tipped employee.”



the value of the credit (the amount that an employer might retain) from 50% down to 45% by January 1, 1979, and to 40% by January 1, 1980.<sup>13</sup>

The student sub-minimum rate had, by this point, become *standard policy*: something of a *tradition* and one that industry wanted to see strengthened. Both in the House and in the Senate, during floor consideration of the 1977 FLSA amendments, proposals were offered to allow, under differing circumstances, for the employment of youth workers and students. Provisions varied as did the nuances of the plan. Usually, it called for full-time students working part-time, but without regard to age, duties, or training. Some urged a more all-encompassing youth rate. Organized labor strongly opposed a more general sub-minimum wage — as did many Members of Congress. The concept was rejected in each house of the Congress — though by exceedingly close margins.<sup>14</sup>

## The 1989 Amendments

In 1989, Congress essentially reversed the 1977 FLSA tip credit amendments. The new amendments provided that the tip credit would rise to 45% as of April 1, 1990, and to 50% after March 31, 1991.<sup>15</sup>

The 1989 amendments also provided another *offset* that industry had long urged. What had been termed a *youth sub-minimum wage* in the 1960s and a *youth opportunity wage* during parts of the 1970s and early 1980s, now became a *training wage*.

Industry had long argued for a different minimum wage for youth workers — notably, with respect to full-time students who worked part-time. The theory of that period (though some disputed it) was that students, because of scheduling problems with classes and sports, would be disadvantaged in the world-of-work and would find it more difficult to secure employment than non-student workers. Thus, if they were cheaper to hire (by paying them at a sub-minimum rate), their employment might more readily be ensured.<sup>16</sup>

As minimum wage legislation moved through the 101<sup>st</sup> Congress, a major issue in each house had been a training wage for youth. The legislation that was initially adopted did not include such a provision. However, President George H. W. Bush was convinced of the utility of a training wage and, in mid-June 1989, vetoed the minimum wage bill — urging that the bill be rewritten to include a more general sub-minimum wage for youth. Negotiations continued through the summer and into the fall at which time new legislation was approved by Congress that, now, contained a

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<sup>13</sup> P.L. 95-151, Section 3.

<sup>14</sup> See CRS Report 78-171, *The Fair Labor Standards Act Amendments of 1977 (P.L. 95-151): Discussion with Historical Background*, by Charles V. Ciccone and William G. Whittaker, Aug. 15, 1978, pp. 62-76. An archived report, available from the author.

<sup>15</sup> P.L. 101-157, Section 5.

<sup>16</sup> The issue had come to be associated with the fast food industry — though it would have applied to any employment sought by young persons.

training wage for youth. The bill was signed by the President on November 17, 1989.<sup>17</sup>

The new training wage was of two parts. *Any employer* could pay a sub-minimum wage to any employee (who “has not attained the age of 20 years” and is “not a migrant agricultural worker or a seasonal agricultural worker”) through “a cumulative total of 90 days” of employment. No training would be required and no consideration of prior experience would need to be taken into account. *The employer* could engage the same employee through a second period of 90 days if certain qualifying types of training were actually given. The training wage was \$3.35 per hour until April 1, 1991, after which it would be \$3.62 per hour (85% of the then-standard \$4.25 per hour minimum wage). The provision was experimental and was to terminate on April 1, 1993 — and it did so.<sup>18</sup>

## The 1996 Amendments

In 1996, revisions of the FLSA differed, somewhat, from earlier measures in that they came to the floor as amendments to an extensive industry-oriented bill, the essence of which had really little to do with standard wage/hour issues. And, thus, they did not have the usual committee oversight.

The tip credit was extended — but, with a difference. The bill provided that the credit (due to employers) would remain at 50% of the minimum wage: i.e., \$2.13 per hour or 50% of the then statutory rate of \$4.25.<sup>19</sup> Then, with the minimum cash wage for tipped employees locked into place, Congress raised the general minimum wage, in steps, to \$5.15 per hour. The result was that the cash wage remained at \$2.13 per hour while the minimum wage escalated. By moving away from a percentage figure (50% of \$4.25 or \$2.13 per hour) to a specific number (\$2.13 per hour to be paid by the employer), there was a decrease in the employer’s statutory obligation to his employees to 41.4% (a \$3.02 credit). The employer would still be

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<sup>17</sup> See “Minimum-Wage Impasse Finally Ended,” *CQ Almanac*, 1989, pp. 333-340; and CRS Issue Brief IB89061, *The Federal Minimum Wage: Consideration in the 101st Congress*, by William G. Whittaker (archived, but available from the author).

<sup>18</sup> The Secretary of Labor was directed to provide Congress with a report on the sub-minimum wage. Secretary Robert Reich reported: “Among employers who had knowledge of the training wage, the most common reason for nonuse was the inability to attract qualified workers at that wage. Administrative burdens and government regulations were also cited as significant reasons for nonuse. Most employers not familiar with the training wage, when informed of the 1989 provision, still said they would not use it.” See U.S. Department of Labor, Employment Standards Administration, Wage and Hour Division (transmitted Apr. 21, 1993), *Report to the Congress on the Training Wage Provisions of the Fair Labor Standards Act Amendments of 1989 from the Secretary of Labor*. See also *Wall Street Journal* editorial, Mar. 12, 1993, p. A4, “Subminimum Wage of \$3.62 an Hour Is on Deathbed but Draws Few Mourners.” As noted above, the student sub-minimum wage, established under the 1961 FLSA amendments, remained in place.

<sup>19</sup> P.L. 104-188, Section 2105(b). The actual wording stated, inter alia: “... shall be not less than the cash wage required to be paid such an employee *on the date of the enactment of this paragraph;...*” (Italics added.)

required to supplement the difference between the \$2.13 per hour and the amount actually earned through tips — if the latter (earnings through tips) were insufficient to make up the difference and, thus, provide a full minimum wage. (See **Table 1**.)

At the same time, Congress approved an “Opportunity Wage” for youth. It affirmed: “... *any employer* may pay any employee of such employer, during the first 90 *consecutive calendar days* after such employee is initially employed by such employer, a wage which is not less than \$4.25 an hour.”<sup>20</sup> The youth *sub-minimum* wage, like the tip credit, was now fixed at a statutory rate: i.e., \$4.25 per hour. Each had become an offset for payment by employers of a minimum wage — and each would prevent many business employers from experiencing the full impact of any subsequent change in the minimum wage.

**Table 1. Federal Minimum Wages for Tipped Employees**

| Jurisdiction   | Basic combined rate: tip and minimum cash wage | Maximum credit: <i>to be retained by employer</i> | Minimum cash wage: <i>to be paid by employer</i> | Definition of tipped employee                  |
|----------------|--|---|--|--|
| Federal (FLSA) | \$5.15   | \$3.02  | \$2.13   | One who earns more than \$30 per month in tips |

This would seem to have several implications. Although widely regarded as a *training wage*, training *per se* was not required. Since youth workers are perceived to move from job-to-job as school or other activities make necessary, it is conceivable that they might remain at the sub-minimum rate through several sequential periods of work — without regard to aggregate experience. And, in labor market areas where work is scarce and young persons are numerous, the primary result would seem to have been to render the youth worker less expensive to employ.<sup>21</sup>

## Current State of Tipped Employment

As currently in force, all workers, regularly covered under Section 6(a)(1) of the FLSA — except for designated sub-minimum wage workers and persons with disabilities — must be paid at least the federal minimum wage.<sup>22</sup> Where the worker

<sup>20</sup> P.L. 104-188, Section 2105(c). Italics added.

<sup>21</sup> Student status is not (necessarily) a qualifier for the new (and present) youth opportunity wage: merely that the candidate be under 20 years of age. Some have suggested that, for seasonal (and often tipped) employment, the 90-day period (three months) would be especially desirable for employers.

<sup>22</sup> The youth/student sub-minimum wage provision is calculated separately, as is a special wage for persons with disabilities. See CRS Report RL30674, *Treatment of Workers with* (continued...)

is *tipped* (earning in excess of \$30 per month in tips), he or she must receive at least \$2.13 per hour directly from the employer — even where the earnings of the tipped employee may be substantially in excess of the minimum wage.

## Combining the State Minimum Wage with the Federal

As was noted above, the first minimum wage laws were adopted by the states. Although the federal government has, since 1938, moved increasingly into the minimum wage field, many of the states still have their own state laws. In some cases, the state standards are higher than the federal and, for that reason, take precedence. In general, where there are conflicting provisions, the higher standard (that perceived to be most nearly in the interest of the worker) prevails.

The tip credit is often viewed as an offset from the minimum wage — enacted as a concession to management. As such, there are a number of states that do not permit utilization of the tip credit. (See **Table 2**.) For an employer operating within these states, a full minimum wage (usually a minimum wage higher than the federal standard) must be paid directly by the employer.

**Table 2. State Law Does Not Permit a Tip Credit to the Employer**

| State or Territory | Qualifiers   | State Minimum Wage Standard |
|--------------------|--|-----------------------------|
| Alaska             | —  | \$7.15                      |
| California         | —  | \$6.75                      |
| Guam               | —  | \$5.15                      |
| Minnesota          |  |                             |
|                    | Large Employer (in excess of \$500,000 in annual receipts) | \$6.15                      |
|                    | Small Employer (under \$500,000 in annual receipts)        | \$5.25                      |
| Montana            |  |                             |
|                    | Large Employer (gross annual sales over \$110,000)         | \$5.15                      |
|                    | Small Employer (gross annual sales at or under \$110,000)  | \$4.00 <sup>a</sup>         |
| Nevada             | —  | \$5.15                      |
| Oregon             | —  | \$7.50                      |
| Washington         | —  | \$7.63                      |

<sup>22</sup> (...continued)

*Disabilities Under Section 14(c) of the Fair Labor Standards Act*, by William G. Whittaker.

**Source:** U.S. Department of Labor, Employment Standards Administration, Wage and Hour Division, Website for Tipped Employees, at [http://www.dol.gov/esa/whd], visited Mar. 1, 2006.

a. The \$4.00 figure is permissible in fields where no higher federal standard applies.

Conversely, some states do permit a tip credit arrangement for certain workers covered under state law. In such cases, several assessments must be made. Does the federal or state standard apply — or, are the workers involved in a field not covered by either federal or state law? Where the minimum wage is \$5.15 per hour (and the worker is covered by federal law), presumably the federal standard would apply. However, in fields that are not covered by federal law, regardless of the wage to be paid, then the applicable portion of the state law — assuming that there is a state law — would take effect. (See **Table 3.**) Some types of work (relatively few) *may* be covered by neither federal nor state laws.

**Table 3. State Law Allows a Tip Credit**

| Jurisdictions            | Basic state combined cash & tip minimum wage rate | Maximum credit: to be retained by employer | Minimum cash wage: to be paid by employer | Definition of tipped employee (monthly unless specified) <sup>a</sup> |
|--------------------------|---|--|---|---|
| Arkansas                 | \$5.15  | 50%  | \$2.575                                   | Not specified   |
| Colorado                 | \$5.15  | \$3.02                                     | \$2.13                                    | More than \$30  |
| Connecticut <sup>b</sup> | \$7.40  | —  | —   | —   |
| Delaware                 | \$6.15  | \$3.92                                     | \$2.23                                    | More than \$30  |
| District of Columbia     | \$7.00  | \$4.23                                     | \$2.77                                    | Not specified   |
| Florida                  | \$6.40  | \$3.02                                     | \$3.38                                    | More than \$30  |
| Hawaii                   | \$6.75  | \$0.25                                     | \$6.50                                    | More than \$20  |
| Idaho                    | \$5.15  | 35%  | \$3.35                                    | More than \$30  |
| Illinois                 | \$6.50  | \$2.60                                     | \$3.90                                    | More than \$20  |
| Indiana                  | \$5.15  | \$3.02                                     | \$2.13                                    | Not specified   |
| Iowa                     | \$5.15  | 40%  | \$3.09                                    | More than \$30  |
| Kansas                   | \$2.65  | 40%  | \$1.59                                    | More than \$20  |
| Kentucky                 | \$5.15  | \$3.02                                     | \$2.13                                    | More than \$30  |
| Maine                    | \$6.50  | \$3.25                                     | \$3.25                                    | More than \$20  |
| Maryland <sup>c</sup>    | \$6.15  | \$3.08                                     | \$3.08                                    | —   |
| Massachusetts            | \$6.75  | \$4.12                                     | \$2.63                                    | More than \$30  |
| Michigan <sup>d</sup>    | \$5.15  | \$2.50                                     | \$2.65                                    | Not specified   |
| Missouri                 | \$5.15  | Up to 50%                                  | —   | Not specified   |
| Nebraska                 | \$5.15  | \$3.02                                     | \$2.13                                    | Not specified   |

| Jurisdictions               | Basic state combined cash & tip minimum wage rate | Maximum credit: to be retained by employer | Minimum cash wage: to be paid by employer | Definition of tipped employee (monthly unless specified) <sup>a</sup> |
|-----------------------------|---|--|---|---|
| New Hampshire               | \$5.15  | 45%  | \$2.38                                    | More than \$20  |
| New Jersey <sup>e</sup>     | \$5.15  | —  | —   | Not specified   |
| New Mexico <sup>f</sup>     | \$5.60  | \$3.47                                     | \$2.13                                    | More than \$30  |
| New York <sup>g</sup>       | \$6.75  | \$2.40                                     | \$4.35                                    | Not specified   |
| North Carolina <sup>h</sup> | \$5.15  | \$3.02                                     | \$2.13                                    | More than \$20  |
| North Dakota                | \$5.15  | 33%  | \$3.45                                    | More than \$30  |
| Ohio <sup>i</sup>           | \$4.25  | 50%  | \$2.125                                   | More than \$30  |
| Oklahoma <sup>j</sup>       | \$5.15  | 50%  | \$2.58                                    | Not specified   |
| Pennsylvania                | \$5.15  | \$2.32                                     | \$2.83                                    | More than \$30  |
| Puerto Rico <sup>k</sup>    | \$5.15  | —  | —   | —   |
| Rhode Island                | \$6.75  | \$3.86                                     | \$2.89                                    | Not specified   |
| South Dakota <sup>l</sup>   | \$5.15  | \$3.02                                     | \$2.13                                    | More than \$35  |
| Texas                       | \$5.15  | \$3.02                                     | \$2.13                                    | More than \$20  |
| Utah                        | \$5.15  | \$3.02                                     | \$2.13                                    | More than \$30  |
| Vermont <sup>m</sup>        | \$7.25  | \$3.60                                     | \$3.65                                    | More than \$30  |
| Virginia                    | \$5.15  | Actual amount received                     | —   | Not specified   |
| Virgin Islands <sup>n</sup> | \$4.65  | 50%  | \$2.33                                    | Not specified   |
| West Virginia               | \$5.15  | 20%  | \$4.12                                    | Not specified   |
| Wisconsin <sup>o</sup>      | \$5.70  | \$3.37                                     | \$2.33                                    | Not specified   |
| Wyoming                     | \$5.15  | \$3.02                                     | \$2.13                                    | More than \$30  |

**Source:** U.S. Department of Labor, Employment Standards Administration, Wage and Hour Division, Website for Tipped Employees, Mar. 1, 2006.

- a. The definition of a “tipped employee” could be misleading. In some cases, more specific earnings levels and related qualifications are indicated. Please see codes of the various states.
- b. Connecticut allows for at least \$10 weekly for full-time employees or \$2.00 daily for part-time employees in hotels and restaurants. The credit varies from one occupation to the next under the cap of \$2.17 per hour.
- c. In January 2006, the Maryland House and Senate voted to override Governor Robert Ehrlich’s veto of a minimum wage increase. Figures, here, represent the new minimum.
- d. At the time this report was being prepared, Michigan was in the process of updating its minimum wage law. It’s possible that a new law will have an impact for tipped employees.
- e. New Jersey’s tip credit varies from a cap of about 40%. Special rates apply mostly to food and related hotel service employees. “The maximum credit is the total amount allowable for tips, food and lodging combined, not for tips alone” as in most other states.
- f. Under New Mexico law, the minimum wage for non-tipped employees is \$5.15 per hour.
- g. In addition, under New York law, the credit varies up to a maximum of \$2.70.

- h. In North Carolina, “[T]ip credit is not permitted unless the employer obtains from each employee, monthly or for each pay period, a signed certification of the amount of tips received.”
- i. In Ohio, the “minimum cash wage for tipped employees of employers with gross annual sales of \$500,000 or less is \$2.01 per hour. For non-tipped employees of such employers, the minimum rates are \$3.35 for employers with sales from \$150,000 to \$500,000 and \$2.80 with sales under \$150,000.”
- j. In Oklahoma, for employers “with fewer than 10 full-time employees at any one location who have gross annual sales of \$100,000 or less, the basic minimum rate is \$2.00 per hour, with a 50% maximum tip credit.” Further, “the listed maximum credit is the total amount allowable for tips, food and lodging combined, not for tips alone” as in most other states.
- k. In Puerto Rico, under the 1966 amendments, most insular rates equal the federal minimum wage rate. However, for the insular tip credit, there is wide latitude based upon individual industries.
- l. In South Dakota, “the listed maximum credit is the total amount allowable for tips, food and lodging combined, not for tips alone” as in most other states.
- m. In Vermont, the listed maximum credit is for employers “in hotels, motels, tourist places, and restaurants who customarily and regularly receive tips for direct and personal customer service.” For all other (basically non-tipped) employees, the minimum wage is \$6.25.
- n. The tip credit in the Virgin Islands applies only to tourist services and restaurant industries. For all other industries, the regular minimum wage rate (\$4.65) applies.
- o. In Wisconsin, there is a state sub-minimum wage standard: “\$2.13 per hour may be paid to employees who are not 20 years old and who have been in employment status with a particular employer for 90 or fewer consecutive calendar days from the date of initial employment.”

In addition, there are several states that do not have state minimum wage standards: i.e., Alabama, Arizona, Louisiana, Mississippi, South Carolina, and Tennessee. In these states, only the federal law applies — which may leave certain low-wage workers, excluded under federal law, without coverage. law.

## Some Potential Complications

The tip credit system can become complex.

Instead of having a single tip (and tax) structure, most states appear to have a system that differs from one state to the next and from the federal system. Singularly, the system may not be overwhelming; but, for firms that operate nationally, it arguably provides one more impediment to business efficiency — especially where the firms are relatively small. Does business necessity require such differences in compensation patterns: i.e., saving a few cents on the minimum wage but with a variety of confusions? Does the system really make sense economically?

For the worker performing minimum wage labor, coping with the system could be daunting. Is he, in fact, subject to the tip credit system? As important, does his employer come under one of the exemptions built into the act (or a state standard) that precludes the necessity of paying a minimum wage at all: e.g., an exemption based upon volume of receipts? Since the minimum wage worker is somewhat more likely to be a part-time employee and/or itinerant, is he in a position to assess the volume of receipts of his or her employer? Where the worker has moved through two or three jobs during a single year, he may be treated differently — and with justification — for wage/hour purposes by each of his employers. If so, can he *really* be sure that he is being treated fairly?

From the perspective of the wage/hour inspector, the system may mean just one more federally mandated requirement. In terms of compliance, the inspector will need to insure that tips are counted, accurately. Can he effectively document the

extent to which income has been offset by tips *actually received*? There is also the issue of reporting to the Internal Revenue Service. (Tips, regularly received, must be reported.) And, finally, how are tips and tip income to be handled for purposes of Social Security?