Notes On: Night of the Living 20% Rule for Tipped Employees

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The so-called "20% Rule" refuses to go away.

In 2018, the Department of Labor ("DOL") issued a revised opinion letter that abolished the 20% Rule and expanded employers' ability to claim the tip credit. The 20% Rule had restricted an employer's ability to claim a tip credit if a tipped employee performed duties that were not tip-producing for more than 20% of the employee's work time. In practice, determining what tasks were tip-producing and attempting to monitor employee activities for compliance with this 20% cut-off proved challenging for most employers of tipped employees. In removing the 20% Rule, the DOL's 2018 guidance provided that employers could take a tip credit for time a tipped employee spends on non-tipped duties, provided those duties are related to the tipped occupation and occur contemporaneously with the tipped occupation or a reasonably immediate time before or after. This guidance provided more certainty and was welcome relief for employers of tipped employees.

But the initial relief was short-lived. Since the DOL's 2018 guidance, some federal courts have continued to apply the 20% Rule, reasoning that the 2018 guidance was not entitled to deference because it significantly conflicted with the longstanding 20% Rule issued by the DOL in guidance three decades earlier. These decisions only created more uncertainty.

Then, on December 22, 2020, the DOL formalized its 2018 guidance and rescinded the "20% Rule" regarding the tip credit through a new Final Rule that revises Fair Labor Standards Act ("FLSA") regulations. By adopting this Final Rule through formal notice and comment rulemaking, if it goes into effect in its current form, courts should afford the DOL a higher level of deference regarding its revocation of the 20% Rule. This was supposed to be the end for the lingering 20% Rule, and employers again believed more certainty was imminent.

But not so fast. Now, the 20% Rule may survive as the new Biden administration and Congress revisit the Final Rule along with other midnight rules passed by the Trump administration. If the Final Rule is withdrawn, modified, or overturned, then the 20% Rule will likely live on.

The FLSA and 1967 Dual Jobs Regulation

The FLSA guarantees non-exempt workers a federal minimum wage of $7.25 per hour. However, employers may pay a "tipped employee" a reduced hourly cash wage so long as that hourly cash wage, plus the tips received by the employee, equals or exceeds the federal minimum wage. The FLSA defines a "tipped employee" as "any employee engaged in an occupation in which he or she customarily and regularly receives not less than $30 a month in tips." 29 U.S.C. § 203(t).

In 1967, the DOL promulgated several regulations addressing the treatment of tipped employees under the FLSA. One of those regulations attempted to delineate when an employee is employed in dual jobs, one tipped and one not. According to that "dual jobs" regulation ("1967 Dual Jobs Regulation"), if an employee works in two different occupations, one of which is tipped and one of which is not, the employer may only take the tip credit for time served in the tipped occupation. The regulations gave the example of a maintenance man at a hotel who also serves as a waiter, explaining that this employee is employed in two occupations, and no tip credit may be taken for his time spent as a maintenance man. The regulation then distinguished that situation from an employee's performance of duties that relate to the tipped occupation but are not themselves directed at producing tips. For example, the regulation provided that a waitress who spends part of her time setting tables or toasting bread is still in a tipped occupation. According to the regulation, the employer may still take the tip credit for all of her time, even if some of her duties are not directed toward producing tips.

After promulgating its regulations regarding tipped employees, the DOL further interpreted the 1967 Dual Jobs Regulation in a revision to its 1988 Field Operations Handbook ("1988 FOH"). It provided that if an employee spent more than 20% of the employee's time, which the 1988 FOH called "substantial," performing tasks related to the tipped occupation but not directed toward producing tips, then no tip credit could be taken for the time spent in those related duties (*i.e.*, the 20% Rule). Furthermore, the 1988 FOH stated that no tip credit could be taken for any time an employee spent performing tasks unrelated to the tipped occupation.

DOL's 2018 Opinion Letter

In a November 8, 2018 Opinion Letter ("2018 Opinion Letter"), the DOL eliminated the 20% Rule in its guidance through reissuance of Opinion Letter FLSA2009-23, which was released in the closing days of the George W. Bush administration but withdrawn by the Obama administration for further consideration.

The 2018 Opinion Letter returned to the text of the FLSA regulations to clarify the definition of a "tipped employee" under the statute. It adopted the FLSA's occupation-focused approach to interpreting the definition. Instead of examining the amount of time an employee spends on so-called related duties, the 2018 Opinion Letter focused exclusively on whether the employee's duties are truly part of the tipped occupation, regardless of how much time an employee spends on any one of them.

To help employers discern what duties are related to a tipped occupation, the 2018 Opinion Letter adopted the Occupational Information Network (O*NET) database to determine what duties are part of that tipped occupation. It stated that an employer may take the tip credit for all of the time an employee spends performing duties listed as "core" or "supplemental" to their relevant tip-producing occupation.[1] The DOL placed no limitation on the amount of these duties, whether or not they involved direct customer service, as long as they were performed contemporaneously with the duties involving direct service to customers or for a reasonable time immediately before or after performing such direct-service duties. The 2018 Opinion Letter favorably cited a 1980 opinion letter that concluded a waitperson's time spent performing related duties (vacuuming) after a restaurant closed was subject to the tip credit.

In contrast, the 2018 Opinion Letter provided that employers could not take a tip credit for time an employee spent performing any tasks not identified on the O*NET task list. However, the 2018 Opinion Letter noted that those tasks may be *de minimis* and therefore not compensable. And in conjunction with its 2018 Opinion Letter, the DOL also revised the Field Operations Handbook to reflect the 2018 Opinion Letter's guidance ("2018 FOH").

By eliminating the 20% Rule and providing such specific guidance as to the types of duties that were and were not covered by the tip credit, the tipped employee playing field was more certain for both employers and employees.

Courts Continued to Apply 20% Rule Despite DOL's 2018 Guidance

Although the DOL abolished the 20% Rule through its 2018 guidance, however, the 20% Rule continued to live on in the courts.

Despite the 2018 Opinion Letter and revised FOH, a number of federal district courts refused to defer to the agency's new guidance and continued to apply the 20% Rule.[2] The *Roberson v. Texas Roadhouse* case is illustrative of the approach courts have taken in continuing to apply the 20% Rule despite the 2018 Opinion Letter rescinding it.[3]

As the *Texas Roadhouse* court explains, courts will generally apply *Chevron* deference[4] to a regulation where Congress has delegated authority to an agency to promulgate a regulation to fill a gap within a statutory scheme. But where the regulation itself is ambiguous, courts will then apply *Auer* deference[5] to agency guidance (such as an opinion letter or field operations handbook) interpreting the regulation if that guidance implicates the agency's expertise and reflects fair and considered judgment of the agency. However, if new agency guidance is an about-face from a prior and longstanding agency position, courts will not afford that new guidance *Auer* deference. When a court determines either *Chevron* or *Auer* deference is appropriate, the agency's interpretation of a statutory scheme is binding on the court.[6]

Following this deference framework, the *Texas Roadhouse* court first determined that the DOL's 1967 Dual Jobs Regulation was entitled to *Chevron* deference because it was properly promulgated within the authority delegated to the DOL to fill in a statutory gap within the FLSA regarding the tip credit. Next, the court held that the 1967 Dual Jobs Regulation was ambiguous because it did not address how much time a tipped employee must spend performing non-tipped duties to make the employee ineligible for a tip credit for compensable time on non-tipped work.

Because the court found an ambiguity within the 1967 Dual Jobs Regulation, the court then analyzed whether any agency guidance warranted *Auer* deference. The court found that the 2018 Opinion Letter and 2018 FOH conflicted with the DOL's longstanding 20% Rule contained within the 1988 FOH. Because the new DOL guidance substantially deviated from the three-decades-old 20% Rule, the court held that the 2018 Opinion Letter and 2018 FOH created an unfair surprise and thus were not warranted *Auer* deference.[7]

Finding the 1967 Dual Jobs Regulation ambiguous and *Auer* deference inappropriate (and thus no agency guidance binding), the court turned to interpreting the 1967 Dual Jobs Regulation on its own. Reasoning that the text of the regulation implied some sort of temporal limit to a tipped employee's performance of non-tipped tipped work, the court held that applying a 20% threshold to non-tipped work was a reasonable interpretation of the 1967 Dual Jobs Regulation.

The recent *Texas Roadhouse* opinion and similar court decisions in the wake of the 2018 Opinion Letter and 2018 FOH have revived the 20% Rule despite the DOL attempting to abolish it in 2018. These cases made clear that the DOL would need to update the 1967 Dual Jobs Regulation itself to obtain heightened *Chevron* deference from the courts and truly rescind the 20% Rule.

The DOL Revises the 1967 Dual Jobs Regulation to Rescind the 20% Rule

In an apparent response to courts' continued application of the 20% Rule, in 2020, the DOL formally revised its regulations to abolish the 20% Rule. On December 22, 2020, the DOL issued a Final Rule that updated the 1967 Dual Jobs Regulation to codify the guidance set forth in the DOL's 2018 Opinion Letter.[8]

Just as provided in the 2018 Opinion Letter, the Final Rule now allows an employer to take a tip credit on time spent by a tipped employee on non-tipped duties if: (1) those non-tipped duties relate to the employee's tipped occupation; and (2) those non-tipped duties are performed contemporaneously with or a reasonable time immediately before or after tipped activities. And, like the 2018 Opinion Letter, the Final Rule adopts O*NET as the source of guidance to determine whether non-tipped duties are related to a tipped occupation.

In explaining the policy reasons for rejecting the 20% Rule in favor of the above related-duties approach, the Final Rule expressed concerns that the 20% Rule placed the difficult administrative burden on employers of categorizing tasks and tracking each employee's time on a minute-by minute basis. The Final Rule states that "[r] emoving the rigid 20 percent limitation, but permitting an employer to take a tip credit for time spent on non-tipped work only when that work is related to the tipped occupation and performed in conjunction with tipped work, reasonably interprets the statutory text while striking a balance that is both protective of employees and manageable for employers." The Final Rule reasons that the related-duties approach, rather than the 20% Rule, is reasonable interpretation of the FLSA because the FLSA allows an employer to take a tip credit if an employee is engaged in a tipped "occupation" and not based on the types of duties or tasks performs within that tipped occupation.

While the Final Rule has not yet been interpreted by courts, if the Final Rule survives, it should hopefully abate the wave of litigation spawned by the 20% Rule that has continued despite the 2018 Opinion Letter and 2018 FOH—relieving employers of the burden of monitoring the minute-by-minute tasks of their employees. Going forward, employers would need to carefully review the job descriptions as well as the actual duties for all employees for whom the employer is claiming the tip credit to confirm that those duties are listed as core or supplemental to the tipped occupation on the O*NET database. Managers would also need to ensure that tipped employees are not asked to perform any duties that are not identified on the O*NET database.

The Biden Administration and Congress Put the Final Rule in Crosshairs

With the change in administrations, however, the Final Rule and any other so-called "midnight rules" (*i.e.*, those regulations and guidance promulgated near the end of a president's term) are vulnerable to actions by the Biden administration or Congress.

On January 20, 2021, President Biden issued a regulatory freeze memorandum affecting midnight rules passed in the final days of the Trump administration. The memorandum asked agencies to not propose any new rules unless approved by the Biden administration, to consider postponing rules that have not gone into effect for 60 days, and to consider opening a new comment period to evaluate rules further. After the postponement, with respect to each affected rule, the memorandum asks agencies to consider taking no action, further delaying the effective date, or taking further action with the Office of Management and Budget, meaning the rule will likely be withdrawn or revised.

In response to President Biden's regulatory freeze memorandum, the DOL has already proposed to delay the Final Rule's effective date from March 1, 2021 to April 30, 2021. This move indicates that the Final Rule is one of the midnight rules that the Biden administration is considering withdrawing or revising. If the Biden administration does withdraw the Final Rule, then courts will likely continue the pattern of enforcing the 20% Rule. And, if the Biden administration withdraws the Final Rule, it will likely withdraw the 2018 Opinion Letter as well. That would remove any ability for employers to argue that *Auer* deference requires that courts disregard the 20% Rule.

But, even if the Biden administration does not withdraw or revise the Final Rule, Congress also has the power to strike down the Final Rule. The Congressional Review Act ("CRA")[9] provides a mechanism for Congress to disapprove of regulations promulgated by agencies within the Executive Branch. Under the CRA, Congress may disapprove a promulgated agency rule with a joint resolution by a simple majority vote. The President may respond by vetoing the joint resolution of disapproval—which means a two-thirds majority vote of both houses of Congress would be required to enact the resolution. If Congress disapproves a regulation (and the disapproval survives the President's veto), the regulation does not take effect or continue, and the agency cannot promulgate a regulation in the future that is substantially the same as the one disapproved.[10]

The CRA gives Congress the authority to disapprove of regulations that were passed within 60 session days of the regulation's promulgation. Based on Congress's schedule, the estimated cutoff date for regulations that could be considered is August 21, 2020. The Final Rule was announced on December 22, 2020 and is thus well within the purview of the CRA.

For employers burdened by the 20% Rule, it would likely be better for the Biden administration to withdraw the Final Rule than for Congress to strike it down using the CRA. The Biden administration withdrawing the Final Rule leaves the door open for a future administration to revoke the 20% Rule again. But, if Congress disapproves of the Final Rule through the CRA, then proponents could argue that the 20% Rule becomes permanent because the CRA prohibits the agency from promulgating the substantially same rule as the Final Rule in the future. However, this aspect of the CRA has not been tested in the courts.[11]

The Final Rule is in danger and the 20% Rule may live on. Employers should continue to try to enforce employee compliance with the 20% Rule and stay tuned to actions taken by the Biden administration or Congress on this Final Rule.

ENDNOTES

1 The relevant duties can be found in the Tasks section of the Details report in the Occupational Information Network (O*NET) database, available at https://www.onetcenter.org. To search occupations within the O*NET database, go to https://www.onetonline.org/.

2 *See, e.g.*, *Kafka v. Melting Pot Rests.*, 2019 U.S. Dist. LEXIS 232407, at *9 (W.D. Mo. Apr. 30, 2019); *Sicklesmith v. Hershey Entertainment*, 440 F. Supp. 3d 391, 402-04 (M.D. Penn. 2020); *Cope v. Let's Eat Out*, 354 F. Supp. 3d 976, 986 (W.D. Mo. 2019); *O'Neal v. Denn-Ohio, LLC*, 2020 U.S. Dist. LEXIS 5721 at *18-23 (N.D. Ohio Jan. 14, 2020); *Reynolds v. Chesapeake & Del. Brewing Holdings, LLC*, 2020 U.S. Dist. LEXIS 83633, at *13 (E.D. Pa. May 12, 2020); *Berger v. Perry's Steakhouse*, 430 F. Supp. 3d 397, 412 (N.D. Ill. 2019); *Rorie v. Wsp2*, 2020 U.S. Dist. LEXIS 166080, at *12 (E.D. Ark. Sep. 9, 2020); *Esry v. P.F. Chang's China Bistro, Inc.*, 373 F. Supp. 3d 1205, 1210 (E.D. Ark. 2019); *Belt v. P.F. Chang's China Bistro, Inc.*, 401 F. Supp. 3d 512, 531 (E.D. Pa. 2019); *Williams v. Bob Evans Rests., LLC*, 2020 U.S. Dist. LEXIS 145852, at *33 (W.D. Pa. Aug 13, 2020).

3 *Roberson v. Tex. Roadhouse Mgmt. Corp.*, 3:19-CV-628-RGJ, 2020 WL 7265860, at *1 (W.D. Ky. Dec. 10, 2020).

[4] *See Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837 (1984).

[5] *See Auer v. Robbins*, 519 U.S. 452 (1997).

[6] Courts may also apply *Skidmore* "deference" to agency guidance where *Auer* deference is not appropriate. *See Skidmore v. Swift & Co.*, 323 U.S. 134 (1944). Under this principle, courts may consider such guidance persuasive but not binding.

[7] Similarly, because of the "stark shift" in policy between the DOL's 20% Rule within the 1988 FOH and the new 2018 Opinion Letter and FOH, the court was not persuaded by the new guidance under *Skidmore* deference.

[8] The Final Rule was not limited to only codifying the 2018 tip credit guidance. For a summary of other aspects of the Final Rule, please see Haynes and Boone Alert: DOL Gives Employers New Nontraditional Tip Pooling Option.

[9] 5 U.S.C. §§ 801 – 808.

[10] 5 U.S.C. § 801(b).

[11] Congress invoked the CRA only once prior to the Trump administration to disapprove an ergonomics rule promulgated by the Clinton administration. To the extent that the number of regulations struck down by Congress under the CRA during the Trump administration are promulgated again by the Biden administration, and then challenged on CRA grounds as being substantially the same, courts could provide guidance on this doctrine.