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## The Case for Tipping and Unrestricted Tip-Pooling: Promoting Intrafirm Cooperation

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# THE CASE FOR TIPPING AND UNRESTRICTED TIP-POOLING: PROMOTING INTRAFIRM COOPERATION

SAMUEL ESTREICHER\*  
JONATHAN REMY NASH\*\*

Abstract: No law in the United States requires or prohibits customers from tipping employees for satisfactory service. Tip income is typically regarded as belonging to employees and may not be appropriated by the employer. Tipping is a widespread phenomenon in certain settings—restaurants, hotels, and gambling casinos. It is a form of performance-based variable compensation that is generally not found elsewhere in this country, where employees generally prefer fixed incomes over a defined period. As a general matter, our laws allow tipping but regulate the sharing of tip income among employees. In the restaurant setting, tip-pooling occurs when tips received by one employee are shared to some extent with other employees. For example, waitstaff at a restaurant might pool tips only with other waiters; this is legally permitted. A broader arrangement, that is presently not allowed, would be an employer policy providing for the sharing of tips beyond the waitstaff to include those who bus the tables or work in the kitchen. The U.S. tipping norm is under challenge. A growing number of restaurant own-

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We discuss in this Article (1) the relative merits of an employer policy allowing and encouraging customers to tip employees for satisfactory service as contrasted with an employer policy dissuading such tipping, and (2) the relative merits of a policy barring the sharing of tips with non-server employees as opposed to a policy allowing such tip-pooling. We leave for another day other important questions concerning tipping, such as whether there should be a subminimum wage for “tipped” employees, and, if so, whether that wage floor should be raised in light of increases in the cost of living or minimum wages. See SYLVIA A. ALLEGRETTO & DAVID COOPER, *ECON. POL’Y INST., TWENTY-THREE YEARS AND STILL WAITING FOR CHANGE: WHY IT’S TIME TO GIVE TIPPED WORKERS THE REGULAR MINIMUM WAGE* 18 (2014); NAT’L ECON. COUNCIL ET AL., *THE IMPACT OF RAISING THE MINIMUM WAGE ON WOMEN: AND THE IMPORTANCE OF ENSURING A ROBUST TIPPED MINIMUM WAGE* 5 & nn.8–9 (2014). We also do not address state and local government laws that may require employers to treat tip income as belonging to employees even where tipped employees are paid the full statutory minimum wage. Cf. *Marlow v. New Food Guy, Inc.*, 861 F.3d 1157, 1159 (10th Cir. 2017) (“If an employer pays more than the minimum wage without regard to tips, the FLSA does not restrict the employer’s use of tips.”).

ers in big cities are moving to ban tipping and instead raise prices. They argue that existing law precludes them from sharing tips with back-of-the-house employees (like chefs and dishwashers), and thus makes it hard to compensate those employees fairly for their contribution to the joint endeavor. We argue that the movement against tipping is ill-advised. Voluntary tipping is a valuable social institution that allows customers to monitor service where management cannot readily do so. The better answer to a flat-out tipping ban is to remove legal restrictions on tip-pooling. Pooling tips among a broad swath of employees (other than ownership-level employees) helps promote the cooperative endeavor underlying the provision of service in settings like restaurants.

## INTRODUCTION

Imported from Europe, tipping grew in popularity across the United States in the first century, and by the early 1900s it was fairly well-established in restaurants, hotels, and railroads.<sup>1</sup> The first half of the twentieth century witnessed growing discomfort with the practice, extending even to the organization of an “Anti-Tipping Society of America.”<sup>2</sup> Some establishments actively discouraged tipping.<sup>3</sup> The anti-tipping movement eventually lost momentum, and tipping became fairly entrenched in American life and culture, at least in restaurants and hotels in big cities, and the gaming industry.<sup>4</sup>

Recently, opposition to tipping has re-emerged. A growing number of restaurateurs have announced their intention to eliminate tipping.<sup>5</sup> It is not always clear what these restaurateurs are, in fact, planning to do. Some may pay all

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<sup>1</sup> See KERRY SEGRAVE, *TIPPING: AN AMERICAN SOCIAL HISTORY OF GRATUITIES 1–7* (1998). Tipping has also become a significant practice for taxicab service, in hair and nail salons, and in the gaming industry. See generally Kandis McClure, *Tip-Pooling at Nevada Casinos*, 5 UNLV GAMING L.J. 81 (2014) (describing tipping practices in the gaming industry).

<sup>2</sup> SEGRAVE, *supra* note 1, at 28–29. Members of the Anti-Tipping Society of America were required not to give a tip to anyone for twelve months, “and to meet possible resultant embarrassment each member is supplied with membership cards which he hands over to such neighbors as may be about him and endeavors to enlist them in the organization.” *Id.* Commercial travelers and businessmen were the principal members of this group, which claimed to have a membership of 100,000 by 1905. *Id.*

<sup>3</sup> See *id.* at 16–17 (noting that the New York Central Railroad actively sought to discourage customers from tipping redcaps, on the ground that the company paid the redcaps directly); THE PETRI-FIED FOREST (Warner Bros. 1936) (featuring a diner scene with the sign “Tipping Is Un-American Keep Your Change” prominently hanging behind the counter).

<sup>4</sup> See SEGRAVE, *supra* note 1, at 59 (noting that from 1920 to 1949 hotels and restaurants that did not allow tips “continued to exist, but in very small numbers”).

<sup>5</sup> Michael Lynn, *Should U.S. Restaurants Abandon Tipping? A Review of the Issues and Evidence*, 5 PSYCHOSOC. ISSUES HUM. RES. MGMT. 120, 121 (2016). A 2015 listing includes the Union Square Hospitality Group, and Dirt Candy in New York City; Bar Marco in Pittsburgh; the Radler in Chicago; Coi and Manos Nouveau in San Francisco; The Walrus and the Carpenter, and Ivar’s Seafood in Seattle; and Victory 44 and Upton 43 in Minneapolis. *Id.* One prominent chain abandoned the experiment in 2016. See Danny Victor, *Joe’s Crab Shack Tried Getting Rid of Tips. It Didn’t Last Long*, N.Y. TIMES (May 12, 2016), <https://nyti.ms/1Wsq31E> [<https://perma.cc/QP7S-8SKF>].

waitstaff at least the statutory minimum wage, and perhaps dissuade diners from leaving tips. In its place, the restaurant would impose a service charge presumably to cover lost tip income to the employees. Others may simply raise waiter pay to the minimum wage without discouraging customer tipping. By paying the minimum wage, the restaurant no longer claims a tip credit on its tax returns; rather, the employer claims a business deduction for wages paid. The underlying motive of the restaurateurs is also unclear.<sup>6</sup> A close observer of tipping practices in the industry argues that tipping overcompensates waitstaff in high-end restaurants and owners may wish to recoup some of these revenues even if prices will have to be raised to partially compensate waitstaff for lost income.<sup>7</sup> Another motive appears to be a desire to implement a more equitable sharing of tip income so it is not exclusively for the benefit of front-of-the-house workers such as waitstaff—who typically come in contact with customers—but can also be shared with back-of-the-house employees such as the people in the kitchen—who do not. Federal and state laws presently constrain such tip-sharing arrangements.<sup>8</sup>

But if the perceived evils are undue restrictions on tip-pooling, it is not clear how a ban on tipping solves the problem. Unless customer perception changes such that waitstaff would no longer receive supplemental income from tipping because customers believe the waiter is now being paid an adequate fixed salary, customers will still tip to some extent. The issue will still arise whether the tips go only to the waiter or whether they may be shared with other employees who contribute to the collective endeavor.

Existing legal rules make it difficult for the employer to adopt what the employer believes to be the best tip-pooling arrangement for its employees. Under present federal law, if the employer wishes to receive a tip credit—to have some of the sums received by employees in tips count toward the statutory minimum wage—the sharing of tips is limited to employees “who customar-

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<sup>6</sup> See Patricia Cohen, *Restaurants Say No to Tips, Yes to Higher Prices*, N.Y. TIMES, Aug. 24, 2015, at A1. Various restaurateurs and managers offered many justifications for considering the elimination of tipping including (1) the growth of the minimum wage, especially in particular states and localities, which forces ownership to give raises to workers who are already receiving amounts far in excess of the minimum wage in tip income; (2) avoiding the “confusing welter of federal, state and local regulations and tax laws” that govern tipping; (3) gaining the freedom “to better calibrate wages to reward employees based on the length of their service and the complexity of their jobs”; and (4) concern over “research showing that diners tend to tip black servers less and that the system can encourage sexual harassment of women.” *Id.*; see also Pete Wells, *Tips Are Going Away at a Prominent Restaurant Group*, N.Y. TIMES, Oct. 15, 2015, at A24; Harriet Alexander, *New Yorkers Bemused by New No-Tipping Policy in Michelin-Starred Manhattan Restaurant*, THE TELEGRAPH (Nov. 22, 2015, 1:48 PM), <http://www.telegraph.co.uk/news/worldnews/northamerica/usa/12009247/To-tip-or-not-to-tip-New-Yorkers-bemused-by-new-dining-diktat.html> [<https://perma.cc/38LE-7S6E>].

<sup>7</sup> Lynn, *supra* note 5, at 152 (“[The] biggest reason for restaurateurs to replace tipping is that it takes revenue away from them in the form of lower prices and gives it to servers in the form of tip income that is excessively high compared to other restaurant employees.”).

<sup>8</sup> See *infra* notes 40–45 and accompanying text.

ily and regularly receive tips.”<sup>9</sup> Management-level employees, including team captains and maître d’s, are excluded, as are back-of-the-house staff such as the employees in the kitchen.<sup>10</sup>

It remains unsettled, however, whether an employer that intends to pay all of its employees the statutory minimum wage, and thus will not be taking a tip credit, may institute a tip-pooling arrangement that allows participation by employees who do not “customarily and regularly” receive tips. The U.S. Department of Labor (DOL), which enforces the federal Fair Labor Standards Act (FLSA), has, since 1989,<sup>11</sup> taken the position that the restriction on who may participate in a tip pool holds whether or not the employer is claiming a tip credit with respect to the recipient of the tip income.<sup>12</sup> But, in 2010, the Ninth Circuit held in *Cumbie v. Woody Woo, Inc.* that the FLSA tip-pooling limitation applies only where employers invoke the tip credit to pay their employees less than the statutory minimum wage.<sup>13</sup> Despite this ruling, in April 2011, the DOL issued regulations reaffirming its tip-pooling restriction.<sup>14</sup> The regulation provides in pertinent part: “[t]ips are the property of the employee whether or not the employer has taken a tip credit under section 3(m) of the FLSA.”<sup>15</sup> In February 2016, the Ninth Circuit held in *Oregon Restaurant & Lodging Association v. Perez* that its decision in *Cumbie* did not bar the DOL’s 2011 regulation, and upheld that regulation as within the agency’s discretion.<sup>16</sup> The Trump ad-

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<sup>9</sup> The Fair Labor Standards Act, 29 U.S.C. § 203(m) (2012) [hereinafter FLSA]; see The Tip Wage Credit, 29 C.F.R. § 531.59 (2017) (“[A]ll tips received by the tipped employee must be retained by the employee except for a valid tip pooling arrangement limited to employees who customarily and regularly receive tips . . .”). On December 4, 2017, the U.S. Department of Labor (DOL) announced it would publish a notice of proposed rulemaking to change this regulation. See *infra* note 17.

<sup>10</sup> See 29 U.S.C. § 203(m)(2) (allowing tip-pooling only for employees who “customarily and regularly receive tips”); *Id.* § 531.59 (same).

<sup>11</sup> See U.S. Dep’t of Labor, Wage & Hour Div., Opinion Letter on Tip Credits/Deductions from Wages (Dec. 26, 1973). The agency’s pre-1989 view was that restrictions on tip-pooling applied only where the employer sought to claim the tip credit. See *id.*

<sup>12</sup> See U.S. Dep’t of Labor, Wage & Hour Div., Opinion Letter on Tip-Pooling (Oct. 26, 1989). Specifically, the letter provides that:

Although section 3(m) concerns the circumstances in which a tip credit can be taken, it also provides guidance on the circumstances in which a requirement that employers contribute a portion of their tips to other employees would be an improper deduction from wages for purposes of compliance with section 6 of the Act.

*Id.* The DOL reasoned that if a tip pool includes employees who do not customarily and regularly receive tips “the employee would, in effect, [be] contribut[ing] part of his or her property to the employer or to other persons for the benefit of the employer, with the result that the employee would not have received the full minimum wage ‘free and clear’ . . .” *Id.*

<sup>13</sup> 596 F.3d 577, 583 (9th Cir. 2010).

<sup>14</sup> 29 C.F.R. §§ 531.52–60 (2011); 76 Fed. Reg. 18,838–45, 18,855–56 (Apr. 5, 2011); see U.S. DEP’T OF LABOR, FIELD ASSISTANCE BULLETIN NO. 2012-2: ENFORCEMENT OF 2011 TIP CREDIT REGULATIONS (Feb. 29, 2012).

<sup>15</sup> 29 C.F.R. § 531.52 (2017).

<sup>16</sup> *Or. Rest. & Lodging Ass’n v. Perez*, 816 F.3d 1080, 1086 (9th Cir. 2016).

ministration DOL has now announced a proposed rulemaking seeking to revise its tip-pooling regulation.<sup>17</sup>

Although we disagree with the Ninth Circuit's ruling, for we do not see a statutory basis in the FLSA for restricting tip-pooling where the employer pays the full statutory minimum wage, this Article proceeds on the normative level.<sup>18</sup> We present below the case for tipping and relatively unrestricted tip-pooling among employees. Our argument is that tipping is a valuable economic practice that can benefit both employees and owners. Tipping helps to solve a principal-agent problem between management and workers. When customers tip based upon the quantity and quality of service, they provide an important feedback mechanism concerning employee performance in circumstances where the employer cannot readily monitor that performance. Tipping facilitates "buyer monitoring."<sup>19</sup> Tip income is related to the size of the overall bill, but it is also a function of customer satisfaction. Employees unhappy with their tips will improve their performance or change jobs.<sup>20</sup> In addition, although this may not provide a complete public policy justification, in settings where cash tips prevail, tipping allows customers (and therefore, if indirectly, employers) to more cheaply reimburse employees for their services.<sup>21</sup> Since cash tips are less likely to be taxed (or at least are likely to be under-reported), the actual benefit to employees is greater than the same amount in (taxable) income would be. In a sense, cash tips allow the customer to distribute income from the public purse to the direct provider of services.

Our fundamental claim is that tip-pooling is a generally desirable practice because it promotes cooperation among employees towards achieving the goals

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<sup>17</sup> On December 4, 2017, the U.S. DOL announced it would publish a notice of proposed rule making to change this regulation. See U.S. DOL, WHD NEWS RELEASE 12/04/2017; OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, RIN 1235-AA21, TIP REGULATIONS UNDER THE FAIR LABOR STANDARDS ACT (FLSA) (2017), <https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201704&RIN=1235-AA21>, [<https://perma.cc/5VRY-BRYE>]. For the DOL's Notice of Proposed Rulemaking, see [www.federalregister.gov/d/2017-12-05/2017-25802](http://www.federalregister.gov/d/2017-12-05/2017-25802).

<sup>18</sup> See, e.g., *Marlow v. New Food Guy, Inc.*, 861 F.3d 1157, 1162 (10th Cir. 2017) (disagreeing with the Ninth Circuit's determination).

<sup>19</sup> Robert J. Kwortnick, Jr. et al., *Buyer Monitoring: A Means to Insure Personalized Service*, 46 J. MARKETING RES. 573, 574 (2009).

<sup>20</sup> The empirical literature suggests, however, that tip income is not always related to customer service. See Michael Lynn, *Tip Levels and Service: An Update, Extension, and Reconciliation*, 44 CORNELL HOTEL & REST. ADMIN. Q., no. 5–6, 2003, at 139, 141; Michael Lynn, *Restaurant Tipping and Service Quality*, 42 CORNELL HOTEL & REST. ADMIN. Q., no. 1, 2001, at 14, 16. Based on this literature, one commentator urges that tipping provides no monitoring, and hence no social benefits. See Yoram Margalioth, *The Social Norm of Tipping, Its Correlation with Inequality, and Differences in Tax Treatment Across Countries*, 11 THEORETICAL INQUIRY L. 561, 581 (2010).

<sup>21</sup> See Samuel Estreicher & Jonathan R. Nash, *The Law and Economics of Tipping: The Laborer's Perspective* 1–2 (Am. Law & Econ. Ass'n Annual Meetings, Paper No. 54, 2004), <http://law.bepress.com/cgi/viewcontent.cgi?article=1068&context=alea> [<https://perma.cc/TYH4-2JA6>].

of the enterprise, and most legal restrictions on tip-pooling are ill-advised.<sup>22</sup> Serving customers is often a cooperative endeavor among several employees only some of whom deal directly with the customer. Tip-pooling arrangements provide a mechanism for employers to reward cooperation among employees. Legal restrictions on tip-pooling preclude employers from putting in place arrangements which would further the shared objectives of all the employees. These restrictions also may fuel friction among employees, only some of whom are legally eligible to participate in tip-pooling.

Not *all* restrictions on tip-pooling should be eliminated. Owners should be barred from appropriating tip income because this would be inconsistent with customer expectations.<sup>23</sup> Customers give tips in the expectation that this income will be distributed to non-owner staff. A clear legal rule enforces that expectation and would yield the maximum benefits of a tipping regime; any ambiguity would discourage tipping. The no-tipping rule operates, in effect, as a bonding device assuring customers that tips will go to the employees.<sup>24</sup> Moreover, the incentive effects of tipping apply to employees not owners. Ownership puts its capital at risk in running the business and enjoys the profit upside. As such, they already have a strong incentive to provide good service.<sup>25</sup> Thus, owners should have no claim to customers' tips—monies that are designed to reward non-management employees for providing quality service.

This Article proceeds as follows. Part I presents doctrinal background. It discusses the laws governing tip-pooling, with an emphasis on relevant federal and state laws.<sup>26</sup> Part II analyzes, from a law-and-economics perspective, how tip-pooling arrangements—both voluntary and mandatory—might arise, and what form they might take.<sup>27</sup> Part III shows how governing law limits the ability of restaurateurs to put tip-pooling arrangements in place, and shapes the incentives of employees.<sup>28</sup> It also analyzes the response of restaurants like the Union Square Hospitality Group that have barred all tipping. Part IV suggests

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<sup>22</sup> See *infra* notes 74–78 and accompanying text.

<sup>23</sup> The line should be drawn to bar non-employee owners and employee owners who have a controlling interest by dint of their ownership share. See RESTATEMENT OF THE LAW, EMPLOYMENT LAW § 1.03 (AM. LAW. INST. 2015).

<sup>24</sup> See Victor, *supra* note 5 (“Company research had found that 60 percent of the restaurants’ customers disliked the change in tipping . . . . They wanted to inspire good service with their tips and they didn’t trust management to pass on the money to its employees . . . .”).

<sup>25</sup> It is at least in part for this reason that, even in establishments where tipping is otherwise customary, the tipping norm does not generally extend to owners who are personally providing the service. See, e.g., Saul Levmore, *Commissions and Conflicts in Agency Arrangements: Lawyers, Real Estate Brokers, Underwriters, and Other Agents’ Rewards*, 36 J.L. & ECON. 503, 532–33 n.55 (1993).

<sup>26</sup> See *infra* notes 30–49 and accompanying text.

<sup>27</sup> See *infra* notes 50–70 and accompanying text.

<sup>28</sup> See *infra* notes 71–73 and accompanying text.



revisions to existing law that would free up management's freedom to utilize tip-pooling.<sup>29</sup>

## I. LEGAL TREATMENT OF TIP-POOLING

In this Part, we provide an overview of the legal treatment of tip-pooling. Section A discusses governing federal law. Section B presents a summary of applicable state laws.

### A. Federal Law

Before we turn to the specifics of federal regulation of tip-pooling, we discuss how and when federal law empowers employers to take advantage of the tip credit, and thus pay less than minimum wage to employees on the assumption that tip income will bring the employees' actual total wages up to—and possibly beyond—the minimum wage.

#### 1. Tip Credit

The tip credit is an exception to the federal minimum wage law. The FLSA<sup>30</sup> establishes a national minimum wage,<sup>31</sup> but sets out a modified standard for so-called “tipped employees”—employees “engaged in an occupation in which [they] customarily and regularly receive[] more than \$30 a month in tips.”<sup>32</sup> Although tipped employees must receive at least the minimum wage, they may receive a portion of their compensation in the form of tips rather than direct wages. Prior to 1966, employers could take a tip credit for up to fifty percent of the statutory minimum wage.<sup>33</sup> In 1996, Congress amended the law to remove the percentage limitation and tie the minimum wage obligation to a fixed amount.<sup>34</sup> Current law sets the minimum non-tip compensation due tipped employees at “the cash wage required to be paid such an employee on August 20, 1996,”<sup>35</sup> i.e., \$2.13.<sup>36</sup> Thus, current law allows more than 70.6%, or \$5.12, of the

<sup>29</sup> See *infra* notes 74–78 and accompanying text.

<sup>30</sup> 29 U.S.C. §§ 201–219 (2012 & Supp. IV 2016).

<sup>31</sup> See *id.* § 206(a)(1). Since 1997, the minimum wage has been set at \$5.15 per hour. The FLSA establishes only a federal wage floor; it explicitly authorizes state and local governments to impose higher minimum wage requirements. See *id.* § 218(a).

<sup>32</sup> *Id.* § 203(t).

<sup>33</sup> See Susan N. Eisenberg & Jennifer T. Williams, *Evolution of Wage Issues in the Restaurant Industry*, 30 A.B.A. J. LAB. & EMP. L. 389, 391 (2015).

<sup>34</sup> See Small Business Job Protection Act of 1996, Pub. L. No. 104-188, § 2105(b), 110 Stat. 1929. The minimum wage in effect from 1991 through October 1, 1996, was \$4.25 per hour. *Kilgore v. Outback Steakhouse of Fla., Inc.*, 160 F.3d 294, 297 (6th Cir. 1998) (citing the 1994 version of 29 U.S.C. § 206(a)). Thus, employers had to provide \$2.13 in minimum cash compensation to tipped employees. *Myers v. Copper Cellar Corp.*, 192 F.3d 546, 548–49 n.3 (6th Cir. 1999).

<sup>35</sup> 29 U.S.C. § 203(m).

<sup>36</sup> Eisenberg & Williams, *supra* note 33, at 391–92.

current \$7.25 federal hourly minimum wage to come in the form of tips.<sup>37</sup> The amount of compensation an employer may provide to a tipped employee in the form of tips and have it count toward the employee's minimum wage is called the tip credit.

The FLSA imposes two requirements an employer must meet in order to take advantage of the tip credit with respect to an employee. First, the employer must advise the employee of its intent to treat tips as satisfying part of the employer's minimum wage obligation. Second, it must allow the employee to retain "all tips received by such employee."<sup>38</sup>

At first blush, one might read the statutory tip credit requirement—that the employer must allow the employee to retain "all tips received by such employee"—as foreclosing the possibility of tip-pooling where a tip credit is sought. The statute, however, expressly provides that it "shall not be construed to prohibit the pooling of tips among employees who customarily and regularly receive tips."<sup>39</sup>

## 2. Restrictions on Tip-Pooling

The DOL and courts have interpreted the FLSA to allow tip-pooling both when voluntarily agreed to by the affected employees and as mandated by employers.<sup>40</sup> In the agency's view, participants in mandatory tipping pools must be employees "who customarily and regularly receive tips."<sup>41</sup> As mentioned,

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<sup>37</sup> *Id.*

<sup>38</sup> 29 U.S.C. § 203(m) (2012).

<sup>39</sup> *Id.*

<sup>40</sup> *See, e.g., Kilgore*, 160 F.3d at 303–04 (concluding that the FLSA "expressly permits the 'pooling of tips' and does not bar employers from requiring tip pooling"). The DOL has taken the position that the size of any mandatory tipping pool must be "customary and reasonable" and that such a requirement is satisfied if employees retain at least fifteen percent of their tips. *Id.* at 302–03 (referring to DOL opinion letters); LES A. SCHNEIDER & J. LARRY STINE, *WAGE AND HOUR LAW: COMPLIANCE AND PRACTICE* § 7:9 (2017). But the Sixth Circuit in *Kilgore* rejected this interpretation as supported neither by the language of the statute or regulations. *See* 160 F.3d at 302–04 (holding that the only valid restriction on mandatory tipping pools is that tipped employees' wages remain at or above the applicable minimum wage).

<sup>41</sup> *See* U.S. DEP'T OF LABOR, WAGE & HOUR DIV., FACT SHEET #15A: OWNERSHIP OF TIPS UNDER THE FAIR LABOR STANDARDS ACT (FLSA) (rev. Dec. 2016), <https://www.dol.gov/whd/regs/compliance/whdfs15a.pdf> [<https://perma.cc/MK7G-E4DH>] (advising that all tips received by the tipped employee are to be retained by the employee except for valid tip-pooling arrangements limited to employees who "customarily and regularly receive tips"). *Compare Kilgore*, 160 F.3d at 301–02 (holding that restaurant hosts at Outback Steakhouses "work in an occupation that customarily and regularly receives tips" and, in doing so, contrasting hosts with "restaurant employees like dishwashers, cooks, or off-hour employees like an overnight janitor who do not directly relate with customers at all"), *with Myers v. Copper Cellar Corp.*, 192 F.3d 546, 550–51 (6th Cir. 1999) ("Because [Copper Cellar] salad preparers did not have any direct intercourse with diners, worked entirely outside the view of restaurant patrons, and solely performed duties traditionally classified as food preparation or kitchen support work, they could not validly be categorized as 'tipped employees' under section 203(m)" and, therefore, could not legally be included in a mandatory tipping pool.).

there is currently a dispute as to whether (1) this bar applies only when employers invoke the tip credit, as some courts have recently held;<sup>42</sup> or (2) this bar is absolute, as DOL regulations maintain.<sup>43</sup> It should be noted that tipped employees enjoy more latitude in crafting voluntary tip-pooling arrangements than employers have in mandating them.<sup>44</sup> States may further restrict employer-mandated tip-pooling, as we discuss below.<sup>45</sup>

### B. State Law

States are free to supplement federal limits on tip-pooling. A few states ban mandatory tip-pooling altogether,<sup>46</sup> although voluntary tip-sharing remains permissible.<sup>47</sup> Other states allow mandatory tip-pooling, but restrict which

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<sup>42</sup> See, e.g., *supra* notes 13–14 and accompanying text.

<sup>43</sup> See 29 C.F.R. § 531.52 (2017).

<sup>44</sup> See SCHNEIDER & STINE, *supra* note 40 (“Despite the[] requirements for involuntary pooling arrangements imposed by [an] employer, employees may enter pooling arrangements with terms which do not conform to these rules if the contributing employees mutually agree to such terms.”).

<sup>45</sup> See *Jameson v. Five Fleet Rest., Inc.*, 131 Cal. Rptr. 2d 771, 776 (Cal. Ct. App. 2003) (“Because [California law] imposes prohibitions on tip-pooling not contained in the FLSA . . . federal authorities . . . are inapplicable.”). “Under [California law], tip-pooling is only permitted among employees who are neither employers nor agents . . . .” *Id.* Some states have statutes that expressly prohibit employer-mandated tip-pooling. See Walter John Wessels, *Minimum Wages and Tipped Servers*, 35 ECON. INQUIRY 334, 336 (1997). Minnesota, for example, prohibits employer-mandated tip-pooling:

No employer may require an employee to contribute or share a gratuity received by the employee with the employer or other employees or to contribute any or all of the gratuity to a fund or pool operated for the benefit of the employer or employees. This section does not prevent an employee from voluntarily and individually sharing gratuities with other employees. The agreement to share gratuities must be made by the employees without employer coercion or participation . . . .

MINN. STAT. § 177.24(3) (2017). Other states are more permissive of mandated tip-pooling. Compare *Matter of Wage & Hour Violations of Holly Inn, Inc.*, 386 N.W.2d 385, 310 (Minn. Ct. App. 1986) (holding that Minnesota “statutes indicate that mandatory tip sharing is not allowed”), with *Leighton v. Old Heidelberg, Ltd.*, 268 Cal. Rptr. 647, 649–53 (Cal. Ct. App. 1990) (holding that California law does preclude employer-mandated tip-pooling), *Fraser v. Pears Co.*, 16 Mass. L. Rptr. 255, 255 (Mass. Super. Ct. 2003) (finding the same result under Massachusetts law), *Wynn Las Vegas, L.L.C. v. Baldonado*, 311 P.3d 1179, 1182 (Nev. 2013) (en banc) (holding that Nevada laws permit employer-mandated tip-pooling where all tips are distributed to employees), and *Alford v. Harolds Club*, 669 P.2d 721, 723–24 (Nev. 1983) (finding the same result under Nevada law).

<sup>46</sup> *E.g.*, KY. REV. STAT. ANN. § 337.065(1) (West 2017) (“No employer shall require an employee to remit to the employer any gratuity, or any portion thereof, except for the purpose of withholding amounts required by federal or state law.”); *id.* § 337.065(3) (“No employer shall require an employee to participate in a tip pool whereby the employee is required to remit to the pool any gratuity, or any portion thereof, for distribution among employees of the employer.”).

<sup>47</sup> *E.g.*, *id.* § 337.065(4) (“Employees may voluntarily enter into an agreement to divide gratuities among themselves. The employer may inform the employees of the existence of a voluntary pool and the customary tipping arrangements of the employees at the establishment.”).

workers may participate in such arrangements.<sup>48</sup> Some states exclude mandatory service charges from treatment as gratuities.<sup>49</sup>

## II. THE INCENTIVES UNDERLYING TIP-POOLING

We consider restaurant tip-pooling under two hypothetical circumstances.<sup>50</sup> First, we consider the setting where the waitstaff themselves decide whether or not to engage in tip-pooling. Then we consider the scenario in which management decides to impose tip-pooling. Our discussion centers on the notion that, whether management mandates tip-pooling or not, the provision of services to restaurant customers is—or at least generally should be—a cooperative endeavor among numerous employees, and the pooling of tips provides a means of rewarding such cooperation.

### *A. Voluntary Tip-Pooling*

If management does not mandate tip-pooling, then the waitstaff themselves may decide whether and, if so, with whom, and to what extent to pool tips. In accordance with standard economic assumptions, we posit as a general matter that in making these decisions waiters seek to maximize their own profits.<sup>51</sup> Under these conditions, we can view the waitstaff at a restaurant as private business people independently providing services to restaurant customers. To be sure, the waitstaff do not compete for individual customers as do, for example, competing restaurants. Rather, the waitstaff serve the customers who choose to patronize the restaurant at which the waitstaff work. Still, we can view each waiter as purchasing food from the restaurant kitchen, which they then resell to the customers seated at their respective tables. The waiter enjoys the profits (in the form of

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<sup>48</sup> *E.g.*, CAL. LAB. CODE § 351 (West 2017). Specifically, the California labor code provides that:

No employer or agent shall collect, take, or receive any gratuity or a part thereof that is paid, given to, or left for an employee by a patron, or deduct any amount from wages due an employee on account of a gratuity, or require an employee to credit the amount, or any part thereof, of a gratuity against and as a part of the wages due the employee from the employer.

*Id.* (emphasis added); *Jameson*, 131 Cal. Rptr. at 776 (interpreting § 351 to preclude not only “employers” from participating in mandatory tip pools, but also employers’ “agents”).

<sup>49</sup> *See Searle v. Wyndham Int’l, Inc.*, 126 Cal. Rptr. 2d 231, 237 (Cal. Ct. App. 2002) (“Because the service charge is mandatory and because the hotel is free to do with the charge as it pleases, the service charge is simply not a gratuity which is subject to the discretion of the individual patron.”).

<sup>50</sup> *See generally* Estreicher & Nash, *supra* note 21, at 15–23 (comparing and contrasting voluntary and mandatory tip-pooling arrangements).

<sup>51</sup> *But see* Cass R. Sunstein, *Human Behavior and the Law of Work*, 87 VA. L. REV. 205, 207 (2001) (“[W]orkers are like most people. They behave like *homo sapiens*, not like *homo economicus*.”).

tips),<sup>52</sup> and decides how to structure restaurant service so as to maximize those profits.<sup>53</sup>

### 1. Degrees of Cooperation

To begin, the waitstaff must decide how much they will cooperate. Saul Levmore, former Dean of the University of Chicago Law School, has offered a framework for determining why firms cooperate with each other under competitive conditions.<sup>54</sup> First, he identifies different degrees of cooperation: explicit cooperation and varying degrees of implicit cooperation, and non-cooperation. He delineates them in the context of two competing firms that purchase like goods on an ongoing basis.<sup>55</sup> Under the model of explicit cooperation, the two competitors might engage in joint venture-like behavior and agree to own and operate a factory from which they both will purchase output.<sup>56</sup> Implicit cooperation arises if the two firms purchase supplies from the same factory, with neither of the competitors having an ownership interest in the factory.<sup>57</sup> Stronger implicit cooperation exists if the factory supplies goods to both competitors but is owned by one of the competitors.<sup>58</sup> Under strict non-cooperation, firms “may refuse to deal with suppliers who deal at all with competitor firms.”<sup>59</sup> A less strict form of non-cooperation envisions firms that “decline to buy components from suppliers who sell identical components to competitors.”<sup>60</sup>

Levmore’s taxonomy of cooperation can be adapted to the restaurant setting. There is a minimal level of cooperation at a restaurant, insofar as the waitstaff have, at a minimum, agreed to work at the same restaurant and offer the same food prepared by the same chefs. To this extent, then, the waitstaff have agreed to cooperate implicitly. Beyond that, the waitstaff remain free to choose a level of cooperation.

An initial decision is whether the waitstaff will agree to engage in what we refer to as “explicit cooperation”—pooling of tips among all waitstaff. In the economic language of firm structure, this is a decision of whether or not to integrate horizontally. If the waitstaff agree to cooperate explicitly, then a subsidiary decision arises—whether or not to pool tips beyond fellow waitstaff

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<sup>52</sup> Cf. Wessels, *supra* note 45, at 334–35 (analogizing “tipping to profit sharing”).

<sup>53</sup> We discuss below the question of how waitstaff might choose whether, and the extent to which, to pool tips. See *infra* note 67 and accompanying text.

<sup>54</sup> See generally Saul Levmore, *Competition and Cooperation*, 97 MICH. L. REV. 216, 216 (1998).

<sup>55</sup> *Id.* at 217–18.

<sup>56</sup> *Id.* at 218.

<sup>57</sup> *Id.*

<sup>58</sup> Levmore describes this option as lying between the first two insofar as “[t]he trading between competitors is now explicit although the investment in the factory was implicitly cooperative.” *Id.*

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

with other restaurant workers, such as the busstaff. Table 1<sup>61</sup> reflects these choices.

*Table 1—Options Under Explicit Cooperation*

|   |
|---|
| Tip-Pooling Restricted to Waitstaff; Other Services Effectively Purchased from Restaurant |
| Tip-Pooling Extended to Other Staff   |

If the waitstaff decide not to pool tips, then, in effect, they will be in competition. At this point, they must decide the degree to which they will implicitly cooperate with one another.<sup>62</sup> First, they might decide simply to share (without delineation) the support staff provided by the restaurant. Under this scenario, the waitstaff would not pool tips with other restaurant staff, and would simply use their services as needed.

A second, less cooperative, option is to have individual members of the waitstaff entice restaurant support staff to provide more (better or faster) service to them by tipping the support staff as they provide services or at the end of each shift. By this, we do not envision a formal tip-pooling arrangement between waitstaff and support staff; rather, waitstaff would provide tips on an ad hoc basis as they see fit. This notion may be of greater applicability with respect to certain support staff services than others. For example, the notion of a waiter tipping a busboy for prompt service on an individual basis might be difficult in practice, but waitstaff at some restaurants do indeed tip the individuals manning the beverage or dessert bars for faster service.<sup>63</sup> Under this scenario, the waitstaff are still using services provided by the restaurant, but they are openly competing with one another for priority with respect to those services.

A third, even less cooperative, option is for the waitstaff to join with particular support staff and form “service teams” that share tips.<sup>64</sup> In the economic language of firms, this scenario is a form of vertical integration. For example, each waiter might choose their own busperson; each team of waiter and busperson would then serve only their own customers, and would pool tips obtained from those customers. Under this scenario—minimal cooperation—the waitstaff cooperate internally only with respect to the provision of foods prepared by the restaurant.

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<sup>61</sup> This Table is permanently available at <http://www.bc.edu/content/dam/bc1/schools/law/pdf/law-review-content/BCLR/58-6/estreicher-nash-graphics-A1b.pdf>.

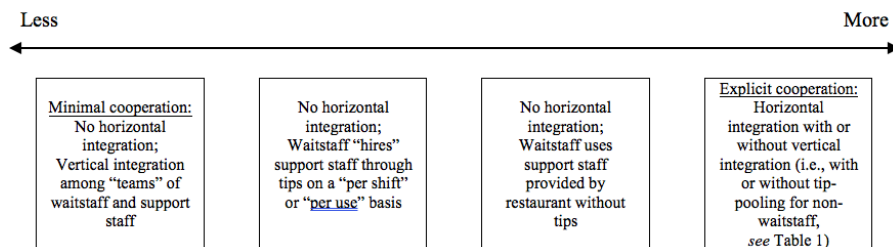
<sup>62</sup> As noted above, there is a minimal level of implicit cooperation, so that non-cooperation is not an option.

<sup>63</sup> Interview with Anonymous Former Dessert Maker at a New York City restaurant, in Tannersville, Pa. (Aug. 3, 2003).

<sup>64</sup> Estreicher & Nash, *supra* note 21, at 17.

Figure 1<sup>65</sup> presents the varying degrees of cooperation, and the resulting staff structures.

*Figure 1—Options Under Varying Degrees of Cooperation*



There is a full spectrum of cooperation possibilities beyond the four distinct options presented in Figure 1. For example, under minimal cooperation, it is possible that waitstaff will offer service to patrons sitting at tables outside their "station" if specifically requested. It is also possible they will absolutely refuse to serve tables outside their station.

## 2. Choosing the Level of Cooperation

Having set out possible degrees of cooperation in which waitstaff might engage, we turn to the question of how waitstaff choose a level of cooperation.

As an initial matter, we think that once a system of tip-pooling or no tip-pooling is in place, that system is likely to remain in place (whether for reasons of inertia or otherwise). But, there are circumstances where employees will opt for tip-pooling. First, the possibility that management might mandate tip-pooling might make voluntary tip-pooling more likely. To the extent management is permitted by law to mandate tip-pooling, the shadow of management compulsion may convince waitstaff simply to come up with an agreement on their own, which they may prefer to whatever arrangement management might impose.

Second, it may be in the economic self-interest of the waitstaff to engage in some tip-pooling entirely on their own, even if management has not mandated the practice. For example, the waitstaff might believe tip-pooling would lead to uniformly better service, which would, in turn, lead to increased patronage and increased tipping, such that all (or virtually all) members of the waitstaff would receive higher pay under a tip-pooling regime.

Third, tip-pooling also addresses employee concerns over horizontal equity<sup>66</sup>—whether similarly-situated employees are being compensated in a rela-

<sup>65</sup> This Figure is permanently available at <http://www.bc.edu/content/dam/bc1/schools/law/pdf/law-review-content/BCLR/58-6/estreichernash-graphics-A1b.pdf>.

tively uniform manner. Employees tend to evaluate satisfaction with their compensation based more upon how their salaries match up with other workers' salaries, than on their salaries' absolute magnitude.<sup>67</sup> Tip-pooling helps ensure that the happenstance of serving a particular customer does not mean significant differences in compensation, and that all employees who engage in the joint venture of serving customers are appropriately compensated for the contribution they make to the overall enterprise. Tip-pooling involves a shift of resources from the waitstaff to the kitchen personnel, which may also compensate for differential status that otherwise might hamper cooperation.

### *B. Mandatory Tip-Pooling*

As noted above, tip-pooling is generally lawful although the class of employee recipients may be limited by law. We explore now the circumstances under which management is likely to require tip-pooling.

At the outset, we assume, as before, that economic self-interest dominates. Accordingly, we assume management seeks to maximize restaurant profits.<sup>68</sup> That means management will implement tip-pooling where such an arrangement will lead to an increase in restaurant profits. It may seem odd to some that management would need to introduce market-like economic incentives *within* a firm. But the fact remains that restaurant employees are engaged in an endeavor that works best under cooperation among waitstaff, and the employer may wish to introduce incentives to ensure that cooperation indeed occurs.

The time horizon over which profits are to be maximized and the type of restaurant involved will affect management's decision. For example, management may simply want to maximize customer turnover so as to increase short-term profits. In that case, management's choice as to tip-pooling will turn on whether the resulting service structure will generate quicker turnover.

Management may be concerned with the perceived quality of service, insofar as it affects repeat business and profits over the longer term. Management may conclude that service is friendlier and more conducive to customer satisfaction in a setting where waitstaff get along well, and may determine that tip-pooling fosters that goal. Certainly, in cases where destructive competitive tipping might occur—that is, tipping designed to encourage waitstaff to pro-

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<sup>66</sup> See generally Joseph J. Cordes, *Horizontal Equity*, in *THE ENCYCLOPEDIA OF TAXATION AND TAX POLICY* 195–96 (Joseph J. Cordes et al., eds., 1999) (explaining the fairness principle that individuals in similar socio-economic situations should be taxed equally).

<sup>67</sup> See, e.g., Robert H. Frank & Cass R. Sunstein, *Cost-Benefit Analysis and Relative Position*, 68 U. CHI. L. REV. 323, 348–49 (2001).

<sup>68</sup> If management and ownership are identical, then the incentive is clear. If management is distinct from ownership, then presumably ownership will reward management for increases in profits, and thus profit-maximization is incentivized.



vide service to higher tippers to the exclusion of lower tippers— management may find it especially appropriate to impose tip-pooling.<sup>69</sup>

Management also may be seeking to maximize profits by minimizing cash salary payments to staff. Recall that tips can be used to offset the cash minimum wage management must pay workers. Thus, if a restaurant pays more of its workers below the generally applicable minimum wage, it may invoke tip-pooling as a means of distributing tips over a greater set of employees.

Management's business plan may also rely on retaining employees over the long term. One aspect of that strategy might be a focus on increasing the attractiveness of lower-tier positions. Tip-pooling provides a mechanism for some improvement in compensation from relatively higher-paid tipped employees to relatively lower-paid non-tipped employees.<sup>70</sup>

As in the case of voluntary tip-pooling, sometimes concerns that are not strictly economic might influence management's decision to mandate tip-pooling, such as a desire to promote horizontal equity among similarly-situated employees. On the other hand, management might be less inclined to implement tip-pooling where waitstaff have been at the position for a considerable period of time; mandating tip-pooling in such circumstances may upset entrenched expectations as to compensation.

### III. THE MISMATCH BETWEEN BANS ON TIPPING AND THE OBJECTIVE OF MINIMIZING RESTRICTIONS ON TIP-POOLING

If the object of a ban on tipping is to shift compensation from relatively higher-paid tipped employees to the relatively lower-paid back-of-the-house staff, the ban is likely to be less direct and less efficient way to promote the stated objective than seeking a relaxation of existing legal constraints on tip-sharing

As discussed earlier, some restaurants are considering banning tipping as a means of shifting more income to back-of-the-house employees.<sup>71</sup> This is a doubtful way to promote a more egalitarian distribution of tip income among employees. If tipping is banned, there is no tip-pooling; there is only management determination of compensation.

We are sympathetic to the frustration of restaurants that are unable, because of legal impediments, to include back-of-the-house employees in tip

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<sup>69</sup> Cf. Saul Levmore, *Norms as Supplements*, 86 VA. L. REV. 1989, 1994 n.7 (2000) (arguing that tipping may influence employees towards "collusion against the employer," such as offering patrons complementary drinks—at the expense of the employer—in order to earn a larger tip).

<sup>70</sup> It may also have a redistributive effect favoring higher-paid employees if some managerial employees are, contrary to federal law, permitted to participate in the pool.

<sup>71</sup> See *supra* note 5 and accompanying text.

pools. Although owners are perfectly free to discourage tipping, we do not believe it is generally in their interest to do so.

A ban on tipping is at counter-purposes with management's objective to promote quality service to customers.<sup>72</sup> The institution of tipping helps solve a key principal-agent problem. The principal (management) is in a poor position to monitor the provision of services to customers; that, in turn, invites agents (employees) to shirk in their provision of services. Tipping mitigates the principal-agent problem by empowering customers—who *can* monitor the provision of services—to reward good service. The elimination of tipping reinstates restaurateurs' principal-agent problem at full bore.

The elimination of tipping leaves in place a substantial principal-agent problem. Unsolved, it is likely to lead to customers having to endure worse service than at other establishments that retain tipping. Additionally, it is debatable whether customers—who are used to having the freedom to tip in order to induce better service—will agree to pay higher prices for food in lieu of the ability to compensate for better service.<sup>73</sup>

#### IV. THE PROBLEMATIC NATURE OF MOST RESTRICTIONS ON TIP-POOLING

Existing law puts severe limits on tip-pooling. Supervisory employees, such as the headwaiter, may not participate in tip pools. Back-of-the-house employees are also ineligible to participate in employer-mandated tip pools. States are also free to bar employer-mandated tip-pooling altogether. We agree that ownership-level employees should be barred from tip-pooling arrangements, but employers should generally be free to mandate tip pools and to include certain supervisory employees, like the *maître d'* and headwaiter, and back-of-the-house employees in those pools, who are directly involved in the provision of service to the customer.<sup>74</sup>

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<sup>72</sup> One commentator questions whether tipping *vel non* affects quality of service. Margalioth, *supra* note 20, at 580. We agree that the average size of tips is more a function of the size of the bill than anything else. But, in our view, the presence of tipping raises the level of quality. It is widely agreed that, in countries where tipping is not customary, such as France, the quality of service is considerably lower than in the United States.

<sup>73</sup> See, e.g., Kathryn Vasel, *Joe's Crab Shack Backs Away from No-Tipping Policy*, CNN MONEY (May 12, 2016, 4:06 PM), <http://money.cnn.com/2016/05/12/pf/joes-crab-shack-ends-no-tipping-policy/> [<https://perma.cc/S9H4-3JPU>] (noting that the restaurant chain was abandoning its no-tipping policy less than a year after it was implemented, based on objections from customers and staff, and loss of business and employees).

<sup>74</sup> Another defensible line—and one that would preclude more individuals from sharing in tip pools—would bar (in addition to owners) executive-level employees. Cf. 29 C.F.R. § 541.100 (2017). An “employee employed in a bona fide executive capacity” is an employee (1) who is paid a rate of no less than \$455 per week; (2) “[w]hose primary duty is” to manage the business—or a “department or subdivision thereof”—in which they are employed; (3) “[w]ho customarily and regularly directs the work of two or more other employees”; and (4) “[w]ho has the authority to hire or fire other employees,” or whose input regarding employee “hiring, firing, advancement, promotion,” etc. has “particular

Consider initially that the delivery of services in this context is a cooperative endeavor. No single employee can provide the full extent of service required by the customer. Yet, while customers are relatively well-positioned to monitor front-of-the-house employees, they are not in a good position to monitor back-of-the-house employees. After all, customers rarely come in contact with back-of-the-house employees, and are rarely able to observe clearly the quality of the services they render. But, front-of-the-house employees are well-positioned to monitor the quality of services back-of-the-house employees render.

The foregoing provides a sound basis for front-of-the-house employees to voluntarily enter tip-pooling arrangements that include back-of-the-house employees. But, our argument here goes further: we posit that owners should be permitted to mandate such arrangements. We offer three justifications for this conclusion.

First, employees are often not well-positioned to decide upon or implement tip-pooling arrangements. Even employees who might otherwise be inclined to share tips face strong inertial forces without the coordinating role of management. Moreover, any tendency for employees acting on their own to favor certain co-workers over others in the tip pool would create friction among employees that could undermine the enterprise as a whole.<sup>75</sup> Management, because it is responsible for the welfare of the enterprise as a whole, is likely to avoid such strains.

Second, owners have put their capital at risk. As such, it makes sense to empower them to create incentives in order to generate the cooperative arrangements they believe will enhance their profits.

Third, limits on tip-pooling restrict management's ability to attract and retain the best employees.<sup>76</sup>

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weight." *Id.* (internal quotation marks omitted). Such a distinction makes sense, insofar as executive-level employees are presumably subject to adequate monitoring by ownership even without tips. In addition, a bar against executive-level employees sharing in tips would arguably accord with employee and customer expectations.

<sup>75</sup> See *Leighton v. Old Heidelberg, Ltd.*, 268 Cal. Rptr. 647, 652 (Cal. Ct. App. 1990) (holding that equitable tip sharing is essential to creating a collaborative and orderly employment environment).

<sup>76</sup> The court in *Leighton* endorsed such an approach by holding that:

To permit a waitress to determine what if anything she should share with the busboy based upon what she deems to be the worth of his service can only lead to the . . . loss of good employees . . . and a disruption in the kind of service the public has a right to expect. An employer must be able to exercise control over his business to . . . provide good service to the public.

*Id.*; see also Jeff Gordinier, *No Tipping, the Danny Meyer Way*, N.Y. TIMES, Nov. 18, 2015, at D8 (noting that a Union Square Hospitality Group restaurant's executive chef "is enthusiastic about the change because it means he will be able to pay his cooks something closer to a living wage, and retain talent"); Alexander, *supra* note 6 (noting that the decision by Danny Meyer to increase menu prices by

We are especially dubious of the DOL's position (which it is now reconsidering)<sup>77</sup> that the FLSA's limitations on mandatory tip-pooling apply even when the employer does not seek to benefit from the tip credit. Employees who are subject to the tip credit earn less than the ordinary minimum wage in direct compensation; insofar as they rely on tips to bring their income up to the standard minimum wage, some restrictions on tip-pooling are warranted to ensure compliance with the minimum wage. But, these restrictions make little sense where employees with customary tips are compensated well above the minimum wage, and no sense where the employer does not claim the tip credit at all. Indeed, there is evidence the restaurant industry is highly-competitive.<sup>78</sup> If so, then imposing restrictions on tip-pooling where the tip credit is invoked may be warranted, but imposing those restrictions where the tip credit is not invoked requires reexamination.

### CONCLUSION

Tip-pooling promotes the objectives of ownership—it is a form of variable pay,<sup>79</sup> compensating employees according to the quality of their services. Tip-pooling is also a form of profit sharing—both in the sense that employees share tips among themselves and in the sense that tipping allows workers to share (if indirectly) in a restaurant's profits. The law should not generally restrict this hybrid form of compensation, other than to make sure owners are not diverting tips to themselves, and tipped employees are at least paid the statutory minimum wage once tips are counted.

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twenty percent “means [that] he is now able to pay his chefs a better salary and [he] has already seen a spike in applications from talented cooks”); Wells, *supra* note 6 (noting that a Union Square Hospitality Group chef “has been agitating for higher pay to attract skilled cooks”).

<sup>77</sup> See *supra* note 9 and accompanying text.

<sup>78</sup> See John E. Anderson & Örn B. Bodvarsson, *Do Higher Tipped Wages Boost Server Pay?*, 12 APPLIED ECON. LETTERS 391, 391 (2005) (finding little evidence of a premium to servers in states with more generous minimum wages); Alex Tabarrok, *The Problem of Contingent Fees for Waiters*, 8 GREEN BAG 2D 377, 379 (2005) (arguing that, even though the tip percentage does not vary with meal price, the fact that the total tip amount does vary with the meal price strongly suggests that the market for servers is highly competitive). *But see* NAT'L EMP'T LAW PROJECT, MINIMUM WAGE BASICS: OVERVIEW OF THE TIPPED MINIMUM WAGE 3 (2015) (presenting data showing that many workers, and in particular many servers, earn less than the standard minimum wage in direct employer compensation); Donald G. Schmitt, *Tips: The Mainstay of Many Hotel Workers' Pay*, MONTHLY LAB. REV., July 1985, at 50, 51 (providing data that shows the extent to which tip income constitutes total wages varies by industry).

<sup>79</sup> See generally MARTIN L. WEITZMAN, *THE SHARE ECONOMY: CONQUERING STAGFLATION* (1984) (endorsing the general desirability of performance-based compensation).

