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Washington Tips and Service Charges Laws: Practical Advice to Avoid Lawsuits

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Tips, Tip Pooling, and Tip Credits

Guidance on Employee Tips

- In Washington state, tip is a voluntary sum of money that a customer freely gives to an employee for services. *See* RCW 49.46 et seq.; ES.A.12.
- Under state law:
 - Employers must pay all tips to employees.
 - The employer may not take tips for company use, or to pay employee wages.
 - “Tip crediting” is not allowed under Washington state law. Tips are **in addition to**, and not a part of, an employee’s state hourly minimum wage. *See* RCW 49.46 et seq.; ES.A.12.



Guidance on Tip Pooling

- Tip pools or tip outs in Washington:
 - Cannot include salaried managers and business owners. Employers, managers, or supervisors may accept tips only for services they directly provide, which should be kept in a separate, individual, tip pool.
 - Can include employees who are not directly serving a customer, such as kitchen staff and hourly lead workers.
 - Must be in addition to, and not a part of, an employee's state hourly minimum wage.
- These rules are the same under federal law, except that under federal law, employers can opt to take a "tip credit," which allows employers to pay less than the minimum wage.
- Employees cannot be required to contribute more than they received in tips to a mandatory tip pool.
- Employees may voluntarily have a tip-sharing agreement. But an employer is not required to assist in administering voluntary tip-sharing agreements.



What About the FLSA?

- The FLSA is federal law and is interpreted by the Department of Labor (“DOL”).
- The DOL recently published a new final rule on September 23, 2021 (86 FR 52973).
- The rule clarifies that while managers or supervisors may not receive tips from mandatory tip pools, managers and supervisors are not prohibited from contributing tips to eligible employees in such pools.
- The rule also provides that the DOL may assess civil money penalties of up to \$1,162 per violation of the FLSA’s tip provisions even if the violations are not repeated or willful. This is significant as DOL civil money penalties as to minimum wage and overtime violations are limited to repeated or willful conduct by an employer.





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Service Charges

Plain Language of the Statute (Minimum Wage Requirements and Labor Standards-RCW 49.46.160)

- (1) An employer that imposes an automatic service charge related to food, beverages, entertainment, or portorage provided to a customer must disclose in an itemized receipt and in any menu provided to the customer the percentage of the automatic service charge that is paid or is payable directly to the employee or employees serving the customer.

- (2) For purposes of this section:
 - (a) "Employee" means nonmanagerial, nonsupervisory workers, including but not limited to servers, busers, banquet attendant, banquet captains, bartenders, barbacks, and porters.
 - (b) "Employer" means employers as defined in RCW 49.46.010 that provide food, beverages, entertainment, or portorage, including but not limited to restaurants, catering houses, convention centers, and overnight accommodations.
 - (c) "Service charge" means a separately designated amount collected by employers from customers that is for services provided by employees, or is described in such a way that customers might reasonably believe that the amounts are for such services. Service charges include but are not limited to charges designated on receipts as a "service charge," "gratuity," "delivery charge," or "portorage charge." Service charges are in addition to hourly wages paid or payable to the employee or employees serving the customer.



Overview of Service Charges

- A service charge is a mandatory fee an employer may charge for services that an employee provides, for instance, mandatory gratuity, delivery fee, etc.
- Customers may believe service charges replace a tip. Because of this, state law requires clear disclosure of who receives the service charge.
- Who must comply? Businesses that provide food, beverage, entertainment, and portering services, such as restaurants, catering houses, convention centers, hotels/motels.
- A surcharge that is not related to services provided by an employee such as a fuel surcharge, late fee, cancellation fee, or parking fee, is not a service charge.



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- Under state law:
 - If a business imposes a service charge, it must clearly disclose on the receipt and menu how much, if any, an employee who provides services will receive from the service charge.
 - If nothing is disclosed, or the disclosure is unclear, then the **entire service charge** must be paid to the employee who provides services to the customer.
 - The service charge paid to an employee is in addition to, and not a part of, an employee's state hourly minimum wage (i.e., tip crediting is prohibited).



Examples of Clear Disclosures

- A service charge of _____%/\$_____ will be added to your bill. _____% of this service charge is paid to the employees who served you today.

OR

- A service charge of _____%/\$_____ will be added to your bill. 100% of this service charge is retained by [Business Name].



Examples of Unclear Disclosures

- The following are examples of unclear disclosure statements, where the entire service charge would be due to the employee:

-A service charge of _____% will be added to your bill.

-A mandatory gratuity of _____% will be added to your bill for parties of _____ or more.

-A delivery charge of \$10.00 will be added to your bill.



Case Law Example

- Hawaii has a state law with similar disclosure requirements as Washington for service charge disclosures on menus, receipts, etc.
- In 2014, a patron (not employee) of a hotel sued, alleging that the hotel where he held his wedding reception did not clearly disclose that the 19% service charge added to the bill was kept by the hotel. *Kawakami v. Kahala Hotel Invs., LLC*, 134 Haw. 352, 341 P.3d 558 (2014).
- The hotel argued that the patron was not informed that the service charge was being kept by the hotel because the service charge was, in fact, being used to pay for the wages and tips of banquet employees through its reclassification system.
- The Court held that the hotel had not followed the plain language of the statute because 15% of the service charge was kept by the hotel as a “management share” to pay for employee wages, even if it was reclassified and distributed to employees. The Court reasoned that the statute was still violated because the hotel used the service charges to pay employee wages.
- The class was ultimately awarded \$269,114.73 in damages.





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Employer Responsibilities

Paying Tips and Service Charges

- **Recordkeeping:** Employers must record the amount paid each pay period to their employee, including tips and the employee's portion of service charges.
- **Payday:** Employers can allow employees to take their tips and service charges when they are earned, or they can provide them on the paycheck covering the same pay period, but no later.
- **Deductions:** The employer cannot deduct cash register shortages or other business expenses from tips or service charges paid to the employee.
- **Processing Fees:** Employers can deduct only a portion of processing fees from tips or service charges paid with a credit or debit card.
 - For example, if a \$10 tip is processed by a company that charges a 1% transaction fee, the employer could deduct 10 cents to cover that portion of the fee.



Taxes on Tips and Service Charges

- Employers are required to withhold taxes from tips and service charges. Employers should only withhold taxes from the amount employees receive from a tip pool – not the amount they put into the tip pool.
- The Internal Revenue Service provides guidance for employees and employers on required recordkeeping related to tips and service charges for federal tax purposes.





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Best Practices

What Should Employers Do?

- Service Charges: Review disclosure statements on menus and receipts to ensure you are disclosing: (1) the total amount or percentage that will be charged to the customer and (2) the portion of the service charge (amount or percentage), if any, that is being distributed to the employee(s) who served the customer.
- Tip Pools: Ensure that no managers, supervisors, or anyone classified as “exempt,” participate in tip pools. If a supervisor works in both supervisory and tipped positions, employers should exercise caution and seek legal guidance as to whether, and under what circumstances, tip-sharing with the supervisor is permitted.
- Consult with experienced legal counsel to adopt policies.







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Attorneys & Counselors

Thank you!

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