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Federal Appeals Court Vacates Department of Labor's "80/20/30 Rule" Regarding Tipped Employees

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On August 23, the United States Court of Appeals for the Fifth Circuit issued its much-anticipated decision in *Restaurant Law Center v. United States Department of Labor*.

In one of the very first federal appellate court rulings since the Supreme Court overruled *Chevron USA Inc. v. Natural Resources Defense Council, Inc.* this year, the unanimous three-judge panel concluded that the Department of Labor's 2021 Final Rule regarding tipped employees and the minimum wage, commonly known as the "80/20 Rule" or the "80/20/30 Rule," is both contrary to the pertinent statutory text and arbitrary and capricious. As a result, the court vacated the rule.

Background: Minimum Wage, the Tip Credit, Dual Jobs, and 80/20

The Fair Labor Standards Act (the "FLSA") allows employers to count a portion of tips received by a "tipped employee" toward satisfying the federal minimum wage obligation. The statute defines a "tipped employee" as "any employee engaged in an occupation in which he customarily and regularly receives more than $30 a month in tips." That portion of the statute has been in place, largely unchanged, since 1966. Whether an employee counts as a "tipped employee" determines whether the employer may pay a reduced hourly wage of as low as $2.13, so long as the tips suffice to make up the difference to minimum wage. Employees who are not tipped employees must receive at least the full minimum wage directly from their employer.

In 1967, the Department of Labor issued a regulation positing that workers may have more than one job with an employer, one of which involves tips and one or more of which does not. The example the Department used was a hotel employee who works some shifts as a server in the hotel restaurant and other shifts as the hotel's maintenance person. The so-called "dual jobs" regulation took the position that the employer may pay the lower hourly wage, known as taking the tip credit, for the time spent in the tipped occupation of server, but not for the time spent in the untipped maintenance occupation.

From the late 1970s to the mid-1980s, the Department issued a series of opinion letters that applied this dual jobs framework to tasks within a *single* occupation, looking specifically at the range of

activities tipped employees like servers perform in restaurants, some of which directly and immediately generate tips and some of which do not. In 1988, the Department revised its internal Field Operations Handbook ("Handbook") to reflect, and to expand on, the results of those various opinion letters. The new provision in the Handbook specified, for the first time, that there are three categories of activity for tipped employees: (1) tip-producing work, like taking a customer's order; (2) activities related to tip-producing work, like re-filling salt and pepper shakers; and (3) activities unrelated to tip-producing work, like taking garbage to the dumpster. The Handbook declared that employers may take no tip credit for time spent on the third "unrelated" category, and that the employer would lose the tip credit for any time spent on the second "related" category if the employee spends more than 20% of the workweek on that type of activity.

That provision in the Handbook remained largely unknown to the public until 2007, when a federal district court in Missouri allowed a claim to proceed past the summary judgment stage premised on an allegation that a restaurant had servers spend more than 20% of their working time on non-tipped tasks while paying the tipped wage instead of full minimum wage. The court relied on the Handbook as legal support for the claim, and the case drew nationwide attention sending shock waves through the restaurant, hospitality, and gaming industries.

This 80/20 concept instantly became very controversial. Beginning in early 2009, the Department engaged in a series of 180-degree reversals of its position. The outgoing Bush administration rescinded the 80/20 rule, only to have the Obama administration reverse that rescission just weeks later. The Trump administration took the step of withdrawing the Handbook provision and issuing a regulation to clarify that 80/20 is not the operative rule, but that regulation did not go into effect before the Biden administration came into office. The Biden administration, in turn, delayed the effective date of the Trump administration's final rule and ultimately withdrew that rule.

In the meantime, the United States Courts of Appeals for the Eighth, Ninth, and Eleventh Circuits upheld various versions of the 80/20 rule. Those courts gave controlling deference to the Department's 1967 dual jobs regulation under *Chevron*, and the Eighth and Ninth Circuits gave controlling deference to the Handbook under *Auer v. Robbins* as the agency's interpretation of its own ambiguous regulation. The Eleventh Circuit considered the issue after the Department had withdrawn the relevant portion of the Handbook, but it concluded that the 80/20 rule flowed directly from the dual jobs regulation itself.

The Department's 2021 80/20/30 Final Rule

In October of 2021, the Biden administration issued a Final Rule of its own. This regulation focused the analysis on the concept of a "tipped occupation," positing that "[a]n employer may only take a tip credit for work performed by a tipped employee that is part of the employee's tipped occupation." Similar to the approach taken in the Handbook, the Final Rule established three categories of activity: (1) directly tip-producing work, such as a server providing table service; (2) directly supporting work, such as setting and bussing tables; and (3) work that is not part of the tipped occupation, such as preparing food.

Under the Final Rule, an employer may take a tip credit for tip-producing work. If an employee spends more than 20% of his or her working time on directly supporting work, the employer cannot take the tip credit for the time *above* 20%. (This differs from the approach in the Handbook, under which an employee who spends 21% of the workweek on this type of activity must receive full minimum wage for the entire time spent on that activity, and not just the portion above 20%.) The Final Rule introduced a new limitation: if an employee spends more than 30 continuous minutes in

directly supporting work, then the employer cannot take a tip credit for time after the first 30 minutes. Hence, the new 80/20/30 moniker. And, as with the Handbook, the Final Rule provides that an employer may not take a tip credit for work that is not part of the tipped occupation.

Litigation Challenging the Final Rule

Shortly after the Department issued the Final Rule, two trade associations, the Restaurant Law Center and the Texas Restaurant Association, filed a lawsuit in the United States District Court for the Western District of Texas challenging the 80/20/30 Rule as contrary to the text of the FLSA as well as being arbitrary and capricious. (In full disclosure, the authors represented the plaintiffs in that case as counsel of record, along with Angelo Amador, the Executive Director of the Restaurant Law Center.) In early 2022, the district court denied the Associations' expedited motion for a preliminary injunction on the sole ground that the court did not believe that there was a showing of irreparable harm. In 2023, the United States Court of Appeals for the Fifth Circuit reversed that ruling, concluding that the Associations had adequately demonstrated irreparable harm and remanding to the district court to address the remaining factors in the injunction analysis.

On remand, the district court once again denied the injunction, this time concluding that the 80/20/30 Rule is valid on the merits. The court also denied the Associations' motion for summary judgment and granted the Department's motion for summary judgment. The Associations appealed to the Fifth Circuit once again.

The Fifth Circuit heard oral argument in April of this year. Not long after the oral argument, the Supreme Court issued its decision in *Loper Bright Enterprises v. Raimondo*, which overruled *Chevron* and directed courts to make their own independent determinations of an agency's authority rather than deferring to agencies.

On August 23, the Fifth Circuit issued its ruling. The court examined the words in the FLSA, focusing on the key phrase "engaged in an occupation," considered a range of dictionary definitions from the era when Congress placed those words in the statute, and concluded that "DOL's interpretation sits uncomfortably with the operative statutory term: 'tipped employee.'" Indeed, as the court observed, "[t]he Final Rule is attempting to answer a question that DOL itself, not the FLSA, has posed." Properly understood, "[t]he FLSA does not ask whether duties composing that given occupation are themselves each *individually* tip-producing." Thus, "[i]n summary, the Final Rule applies the tip credit in a manner inconsistent with the FLSA's text. . . . We must therefore conclude that the Final Rule is 'not in accordance with law'" under the Administrative Procedure Act.

In addition, the court "conclude[d], for reasons similar to those explained above, that the Final Rule is also arbitrary and capricious." The court acknowledged that the FLSA may allow room for the Department to engage in line-drawing with respect to identifying what an "occupation" is or what it means to be "engaged in" an occupation under the statute. But the Final Rule, which focuses on the non-statutory term "tipped occupation" and focus on tips rather than occupations, "is arbitrary and capricious because it draws a line for application of the tip credit based on impermissible considerations and contrary to the statutory scheme enacted by Congress."

Having concluded that the 80/20/30 Rule is invalid, the Fifth Circuit concluded that the proper remedy is to vacate the Rule. The court therefore reversed the district court's summary judgment rulings, rendered summary judgment for the Restaurant Law Center and the Texas Restaurant Association, and vacated the Final Rule.

What Does This Mean for Businesses?

The court's ruling means that the Department's regulation is a nullity. It is possible, though somewhat unlikely, that the Department will petition for further review in the form of panel rehearing, rehearing en banc, or petition for certiorari to the United States Supreme Court. It is also important to keep in mind that some states and localities may have their own standards similar or analogous to the 80/20 concept, and employers must comply with all applicable employment standards, not just federal law.

There is also at least some risk that courts within the Eighth, Ninth, and Eleventh Circuits, which had previously upheld earlier versions of the 80/20 rule, will continue to adhere to that view notwithstanding the Fifth Circuit's clear rejection of those rulings. Because those decisions relied, at least in part, on *Chevron* deference to the 1967 dual jobs regulation and *Chevron* no longer represents the controlling framework for analyzing regulations, those courts should no longer consider themselves bound by the earlier decision upholding 80/20. Indeed, the Eighth and Ninth Circuit rulings hinge mainly on *Auer* deference to a provision of the Handbook that no longer exists, and that the Department replaced with a section premised entirely on the now-vacated 2021 Final Rule. Indeed, the continuing validity of *Auer* itself is in doubt after *Loper Bright*. But, there may be room for further litigation while that issue works its way through the courts. If one or more of those circuits continues to adhere to 80/20, the matter could end up before the Supreme Court.

But for most businesses with tipped employees, this ruling means that it is time to exhale. There will likely be very few, if any, further lawsuits asserting federal minimum wage claims based on supposedly non-tipped work, and the cases that are already on file will probably see plaintiffs' counsel eager to exit the matters. There is no longer an obligation under federal law for employers to maintain records of time spent on various categories of tasks within a single occupation.

More generally, this case shows that when a federal agency like the Department of Labor issues a regulation or other standard that affects your business, and it appears that the agency's action exceeds its authority or otherwise violates the law, you are not powerless. The courts stand ready to rein in agency excesses, and litigation, including directly by businesses or through trade associations, like the Restaurant Law Center created specifically for this purpose, can in appropriate cases lead to justice. Litigation is not inexpensive, and it's not for everyone, but it can be a powerful tool to protect your rights.

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