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UNITED STATES DISTRICT COURT

DISTRICT OF OREGON

PORTLAND DIVISION

OREGON RESTAURANT AND LODGING ASSOCIATION, a Non-profit Oregon Corporation, **WASHINGTON RESTAURANT ASSOCIATION,** a Non-profit Washington Corporation, **ALASKA CABARET, HOTEL, RESTAURANT & RETAILERS ASSOCIATION**, a Non-profit Alaska Corporation,

Case No.:_____

COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF

NATIONAL RESTAURANT ASSOCIATION, a Non-profit Illinois Corporation, **DAVIS STREET TAVERN, LLC**, an Oregon Limited Liability Company, and **SUSAN PONTON**, an individual,

Plaintiffs,

v.

HILDA L. SOLIS, Secretary of the United States Department of Labor, in her official capacity, **NANCY LEPPINK,** Deputy Administrator of the United States Department of Labor, in her official capacity, and **UNITED STATES DEPARTMENT OF LABOR,**

Defendants.

COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF

Plaintiffs Oregon Restaurant and Lodging Association ("ORLA"); Washington Restaurant Association ("WRA"); Alaska Cabaret, Hotel, Restaurant & Retailers Association ("Alaska CHARR"); National Restaurant Association ("NRA") (collectively referred to as "Plaintiff Associations"); Davis Street Tavern, LLC; and Susan Ponton (all Plaintiffs collectively referred to as "Plaintiffs") seek declaratory and injunctive relief against Defendants Hilda L. Solis, in her official capacity as Secretary of Labor, Nancy Leppink, in her official capacity as Deputy Administrator of the Wage and Hour Division ("WHD") of the United States Department of Labor, and the United States Department of Labor ("DOL" or the "Department") (collectively, "Defendants"). Plaintiffs allege and aver as follows:

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PRELIMINARY STATEMENT

1. This is an action by a restaurant employee, a restaurant owner/employer, and restaurant associations whose members comprise restaurant owners/employers. This action is brought pursuant to the Administrative Procedure Act, 5 U.S.C. §§ 500-706 (the "APA"), challenging DOL's 2011 amendments to 29 C.F.R. §§ 531.52, 531.54 and 531.59 (76 Fed. Reg. 18832 *et seq.*) (April 5, 2011) (the "2011 Regulations") purporting to interpret the Fair Labor Standards Act of 1938, as amended, 29 U.S.C. §§ 201-219 (the "FLSA").

2. In 2008, DOL issued a Notice of Proposed Rulemaking presenting for comment a number of proposed changes to various provisions of DOL's regulations interpreting the FLSA. *Updating Regulations Issued Under the Fair Labor Standards Act*, 73 Fed. Reg. 43654 (July 28, 2008) (hereinafter referred to as "2008 NPRM").

3. In 2010, the Ninth Circuit held in *Cumbie v. Woody Woo, Inc.* that "the plain text of the third sentence [of section 203(m)]. . .imposes *conditions* on taking a tip credit and does not state freestanding *requirements* pertaining to all tipped employees." 596 F.3d 577, 581 (9th Cir. 2010)(emphasis in original) (citing FLSA section 3(m), 29 U.S.C. §203(m) (hereinafter referred to as "section 3(m)").

4. In April 2011, DOL issued its 2011 Regulations. *Updating Regulations Issued Under the Fair Labor Standards Act*, 76 Fed. Reg. 18832 (Apr. 5, 2011). Styled as a Final Rule to the 2008 NPRM, and announced as effective 30 days after publication, the 2011 Regulations state DOL's disagreement with the Ninth Circuit's holding in *Woody Woo* and purport to overrule that decision by declaring, among other things, that "tips are the property of the employee whether or not the employer has taken a tip credit under section 3(m) of the FLSA.

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The employer is prohibited from using an employee's tips, whether or not it has taken a tip credit." 29 C.F.R. § 531.52.

5. Shortly after DOL published the 2011 Regulations, the NRA and other entities asked DOL to reconsider applying section 3(m)'s tip credit provisions against employers who pay their employees at least full minimum wage and do not take a tip credit.

6. On June 17, 2011, United States Senator Jeffrey Merkley (D Oregon) wrote a letter to Defendant Leppink regarding "significant concerns from restaurant owners and managers in Oregon" about the 2011 Regulations being "in conflict with [the *Woody Woo*] Decision." Senator Merkley explained that "this lingering conflict leaves employers in Oregon and throughout the 9th Circuit in a state of legal uncertainty." Accordingly, Senator Merkley asked the Department to "provide clarification to employers in the 9th Circuit with regard to what portions of the new rules do and do not apply" and to "offer guidance on what is required of these employers in order to maintain compliance with the FLSA."

7. On November 16, 2011, DOL responded to Senator Merkley with a letter explaining that "the Department is currently developing guidance with respect to the concerns you raise."

8. On February 29, 2012, DOL announced its intent to enforce its 2011 Regulations "addressing ownership of employee tips under section 3(m)" and applying its tip pool limitations "uniformly across the country, including in states covered by the Ninth Circuit." *DOL Field Assistance Bulletin No.2012-2* (Feb. 29, 2012). Shortly thereafter, DOL began contacting employer organizations, including some of the Plaintiff Associations, as well as worker advocacy groups, alerting them of its enforcement position on this matter.

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9. In March 2012, and in subsequent conversations, the NRA again formally asked DOL to reconsider its position on this issue, to withdraw its February 29 Bulletin, and to clarify that employers in the Ninth Circuit who pay their employees the full minimum wage and do not take a tip credit may legally implement tip pools that adhere to the *Woody Woo* decision.

10. On April 26, 2012, DOL hosted an informational conference call attended by representatives of the Plaintiff Associations and other entities, in which DOL confirmed its intent to enforce the 2011 regulations against employers who pay employees a full minimum wage and do not take a tip credit, including all employers in the Ninth Circuit.

11. An underlying issue concerning the conflict between the *Woody Woo* decision and the 2011 Regulations is Defendants' position that only certain employees who work in restaurants meet section 3(m)'s language of "customarily and regularly tipped employees" and who therefore can be in a tip pool. Defendants take the position that only such employees as servers, hosts, bartenders, bussers, and bar-backs (commonly referred to as "front-of-house" employees) can be in a tip pool, but that such employees as cooks, expediters (those who ensure the food gets to the correct guest, in a timely and presentable fashion), and dishwashers (commonly referred to as "back-of-house" employees) are prohibited from being in a tip pool. Based on the *Woody Woo* decision, this distinction would not apply when an employer pays its employees at least full minimum wage and does not take a tip credit; at least all non-management employees would be entitled to share in a tip pool. Based on the 2011 Regulations, however, this distinction would apply regardless of whether the employer pays its employees the full minimum wage and takes a tip credit.

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12. As a direct and proximate result of Defendants' 2011 Regulations and their announced enforcement of them against employers with tip pools in compliance with the *Woody Woo* decision, Plaintiffs and their members who pay their employees at least full minimum wage and do not take a tip credit must change their tip pooling policies to comply with the 2011 Regulations despite the Ninth Circuit's *Woody Woo* decision. If they fail to do this, such establishments risk an enforcement action by DOL or a private lawsuit. Such establishments will incur significant costs, both economic and non-economic, by changing their current tip pooling policies to comply with the 2011 Regulations or, in the alternative, by defending their practices in the event they are subject to a private lawsuit or a DOL enforcement action. Moreover, if the 2011 Regulations are not struck down, individual back-of-house employees are precluded from participating and sharing in tip pools that are in compliance with the *Woody Woo* decision, and even front-of-house employees such as Plaintiff Susan Ponton may not participate in an employer-directed tip pool to share their tips with back-of-house employees even if, like Susan Ponton, it is their desire and choice to do so.

PARTIES

13. Plaintiff ORLA, founded in 1934, with its principal offices in Wilsonville, Oregon, is an Oregon non-profit corporation that advocates for Oregon's food and hospitality businesses on a local, state, and national level. ORLA's mission is to advocate, protect, educate, and promote the foodservice and lodging industry. ORLA is the leading business association for the foodservice and lodging industry in Oregon, and the largest organization of restaurants in Oregon. ORLA represents over 3,500 members, and advocates for over 9,000 foodservice locations and 2,500 lodging establishments in Oregon. In this capacity, ORLA represents its

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members and their interests before the Oregon Legislature, Executive Branch, and courts on matters that impact its members, and works to help its members build customer loyalty, find financial success, and provide rewarding careers in the Industry. By lobbying legislators, monitoring state and federal agencies, supporting political candidates, and assisting in court cases, ORLA ensures that its more than 3,500 member establishments are well-represented in all aspects of government. Many ORLA members are restaurants that do not take a tip credit against the federal minimum wage, and many members have established mandatory tip pools that include back-of-house employees, in accordance with the *Woody Woo* decision. Many ORLA members are small entities as defined by 5 U.S.C. § 601(6).

14. Plaintiff WRA, founded in 1929, with its principal offices in Olympia, is Washington's largest and leading trade association representing the Industry. In this capacity, the WRA represents its members and their interests before the Washington Legislature, Executive Branch, and in courts on matters that impact its members. The WRA also works to help its members build customer loyalty, find financial success, and provide rewarding careers in the Industry. The WRA has over 5,000 restaurant Industry unit members, of which more than 40% are full-service restaurants. WRA members are restaurants that do not take a tip credit against the federal minimum wage, and many members have established mandatory tip pools that include back-of-house employees, in accordance with the *Woody Woo* decision. Many WRA members are small entities as defined by 5 U.S.C. § 601(6).

15. Plaintiff Alaska CHARR, founded in 1964, with its principal offices in Anchorage, is Alaska's largest and leading trade association representing the Industry. In this capacity, the Alaska CHARR represents its members and their interests before the Alaska

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Legislature, Executive Branch, and in courts on matters that impact its members. Alaska CHARR also works to help its members build customer loyalty, find financial success, and provide rewarding careers in the Industry. The Alaska CHARR has over 300 restaurant Industry unit members, of which approximately 150 are full-service restaurants. Alaska CHARR member restaurants do not take a tip credit against the federal minimum wage, and many members have established mandatory tip pools that include back-of-house employees, in accordance with the *Woody Woo* decision. Many Alaska CHARR members are small entities as defined by 5 U.S.C. § 601(6).

16. Plaintiff NRA, founded in 1919, with its principal offices in Washington, D.C. and Chicago, Illinois, is the largest and leading national trade association representing the restaurant and foodservice industry (the "Industry") in the United States. In this capacity, the NRA represents its members and their interests before Congress, the Executive Branch, and in the courts on matters that impact its members. The NRA works to help its members build customer loyalty, find financial success, and provide rewarding careers in the Industry. The NRA has over 435,000 Industry unit members, which includes restaurants and foodservice organizations, suppliers, educators and non-profit organizations. Virtually all state restaurant associations, including the other Plaintiff Associations, have agreements with NRA to share members. Therefore, all restaurant members of the other Plaintiff Associations are also members of the NRA. Many NRA restaurant operator members employ tipped employees, and many have their employees participate in a mandatory tip pool / tip share system that is now called into question by the 2011 Regulations. Many NRA members are small entities as defined by 5 U.S.C. § 601(6).

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17. Plaintiff Davis Street Tavern is an LLC created under Oregon law in 2008, with its principal place of business in Portland, Oregon. Plaintiff Davis Street Tavern owns and operates a full-service restaurant located in Portland, Oregon. Davis Street Tavern's non-management restaurant employees are all paid above the federal minimum wage, and they currently participate in a mandatory tip pool / tip share system in which a percentage of tips received by customers is shared with back-of-house employees, including cooks and dishwashers. Nobody in the tip pool is a member of management. Davis Street Tavern does not take any portion of employee tips for its own use or as part of its own receipts, other than to offset fees charged by credit card companies to convert charged tips into cash, as permitted by DOL. Davis Street Tavern is a member of ORLA and the NRA.

18. Plaintiff Susan Ponton is a resident of Portland, Oregon and an employee of Plaintiff Davis Street Tavern, where she works as a server and earns Oregon minimum wage plus tips. Plaintiff Ponton requested that Davis Street Tavern's mandatory tip pool include the back-of-house employees, to reward them for their contribution to guest service and tips left by guests. Plaintiff Ponton participates in Davis Street Tavern's mandatory tip pool under which a percentage of tips left by guests is shared with back-of-house employees.

19. Defendant Hilda L. Solis (the "Secretary") is the Secretary of Labor, the cabinet-level officer who leads the U.S. Department of Labor. Congress has granted the Secretary the power to administer and to enforce the FLSA. The Office of the Secretary of Labor is located in the Department of Labor in Washington, D.C. Plaintiffs sue the Secretary in her official capacity.

20. Defendant DOL is the federal department charged with administering and enforcing the FLSA. *See* 29 U.S.C. § 204. Congress also granted DOL specifically defined

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authority to promulgate regulations interpreting the FLSA, after providing for public notice and an opportunity for public hearings, and meeting other requirements. *See* 29 U.S.C. § 213(a)(1). DOL is headquartered in Washington, D.C.

21. Defendant Nancy Leppink (the "Deputy Administrator") is the Deputy Administrator of DOL's Wage and Hour Division. The FLSA authorizes the creation in DOL of a Wage and Hour Division under the direction of an Administrator. *See* 29 U.S.C. § 204. Because the position of Administrator presently is vacant, the Deputy Administrator is responsible for promulgating the final amendments to regulations interpreting and implementing the FLSA published by Defendants on April 5, 2011. The Office of the Deputy Administrator is in WHD, in DOL in Washington, D.C. Plaintiffs sue the Deputy Administrator in her official capacity.

JURISDICTION AND VENUE

22. Plaintiffs bring this action under the APA, 5 U.S.C. §§ 500-706.

23. Jurisdiction is proper in this Court pursuant to 28 U.S.C. § 1331 and 5 U.S.C. § 702.

24. Venue is proper under 28 U.S.C. § 1391(e) in that (a) the Defendants include an agency of the United States and employees of that agency acting in their official capacity; (b) Plaintiffs ORLA, Davis Street Tavern and Susan Ponton reside in this judicial district; and (c) no real property is involved in this action.

25. This Court can grant declaratory and injunctive relief under the Declaratory Judgment Act, 28 U.S.C. § 2201 (declaratory judgment) and 28 U.S.C. § 2202 (injunctive relief), as well as 5 U.S.C. §§ 701 et seq., for violations of, *inter alia*, the APA, 5 U.S.C. § 706.

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26. This Court is authorized to grant Plaintiffs' Prayer for Relief and to award costs, including a reasonable attorney's fee, under 28 U.S.C. § 2412 and 5 U.S.C. § 504.

STANDING

27. Plaintiff Davis Street Tavern has standing to bring this litigation.

28. Davis Street Tavern pays its employees at least the full Oregon state minimum wage, outside of any tips the employees receive per its tip pool, and does not take a tip credit against its employees' minimum wage. At the request of its servers, Davis Street Tavern has been operating a mandatory tip pool that includes members of the back-of-house staff for approximately two years, and still is operating such a mandatory tip pool.

29. In light of DOL's 2011 Regulations, and its recent declaration that it will enforce these regulations against employers who pay their employees the full minimum wage and do not take a tip credit against the federal minimum wage, Davis Street Tavern is now forced to either change its tip pooling practices expressly declared lawful by the Ninth Circuit in *Woody Woo*, or to risk an enforcement action by DOL or a private lawsuit. Accordingly, and as presented in the facts throughout this Complaint, Davis Street Tavern will suffer direct and substantial harm if the requested remedies are not granted.

30. Plaintiff Ponton has standing to bring this action.

31. Plaintiff Ponton, a server at Davis Street Tavern, requested to have the restaurant's mandatory tip pool include back-of-house employees, to recognize the fact that such employees' performance directly impacts customer service and the tips left by customers. Plaintiff Ponton benefits from having back-of-house employees in the tip pool, as this arrangement results in more camaraderie between the front-of-house and back-of-

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house employees, leads to greater teamwork between all employees, and ensures back-of-house employees are rewarded for their efforts by being able to share in tips left by customers, which she desires.

32. In light of DOL's 2011 Regulations, and its recent formal declaration that it will enforce these regulations against employers who pay their employees the full minimum wage and do not take a tip credit against the federal minimum wage, Plaintiff Ponton is now prohibited by DOL's stated enforcement policy from continuing to participate in the form of a tip pool that she advocated for and believes is most equitable to all employees whose service impacts customer service. As a result, Plaintiff Ponton will be prohibited from continuing to enjoy the benefits from this form of a tip pool, including increased camaraderie between front-of-house and back-of-house employees, a higher level of teamwork among the employees and a higher level of service to customers as a result–all of which directly results in higher tips for Ponton and the rest of the employees. Accordingly, and as presented in the facts throughout this Complaint, Plaintiff Ponton will suffer direct and substantial harm if the requested remedies are not granted.

33. Plaintiff Associations have standing to bring this litigation.

34. Plaintiff Associations' members have restaurant locations in Washington, Oregon, and Alaska. Those states' current laws require employers to pay employees a state minimum wage that is higher than the current federal minimum wage, and prohibit employers from taking a credit against the minimum wage for tips given to employees.

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35. By operation of these states' laws and the Ninth Circuit's *Woody Woo* ruling, employers in these states can lawfully implement tip pools that require the sharing of tips with back-of-house employees.

36. Many of the Plaintiff Associations' members who have operations in Oregon, Washington or Alaska (and, as to the NRA, in any other state where the employer is either required by state law or decides to pay its employees the full federal minimum wage and not take the tip credit) have suffered and will continue to suffer direct harm as a result of DOL's 2011 Regulations and announced enforcement policy of those Regulations.

37. For example, by changing their tip pool practices to exclude back-of-house employees to comply with the 2011 Regulations, the Association's members and Davis Street Tavern will experience lower morale by individuals removed from the tip pool, turnover of people in the positions removed from the tip pool, and related costs. Moreover, Plaintiff Association members and Davis Street Tavern will incur the direct cost of increasing the wages of the employees who are taken out of the tip pool, to supplement their loss of tips. This will result even if those employees are already being paid at or above market rates because, regardless of their wages, they will lose money by being taken out of the tip pool, which will need to be supplemented or their standard of living will be directly affected.

38. Accordingly, many of the Plaintiff Associations' members have standing to bring this suit in their own right. Therefore, the Plaintiff Associations may bring this action on behalf of those members.

39. None of the claims asserted through this lawsuit, or the relief requested, requires direct participation of Plaintiff Associations' members.

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DAVIS STREET TAVERN SERVERS ASKED TO HAVE BACK-OF-HOUSE EMPLOYEES INCLUDED IN THE TIP POOL

40. When the owners of Davis Street Tavern opened the restaurant in 2008, they instituted a mandatory tip pool that was limited to front-of-house employees such as servers, bartenders, hosts, and bussers.

41. In approximately 2010, Plaintiff Ponton approached management, explaining that she and the other servers wanted to include back-of-house employees in the restaurant's mandatory tip pool. Plaintiff Ponton and the other servers wanted to do this because they did not think it was fair that they made approximately twice as much per hour as the back-of-house employees (once you include their share of the tip pool). Plaintiff Ponton and the other servers also made this request because they believe that the back-of-house employees earn, and are entitled to receive, a portion of the tips left by customers, since their performance also directly impacts customer service and, as a result, customer tips. For example, customers typically are not going to leave as much of a tip if their food comes out late, cold or not in accordance with the guest's specific requests, or if the food comes out on dirty plates or with dirty silverware or glassware.

42. Management met with the front-of-house employees to ensure this is what they wanted. The consensus of the group was that they wanted the back-of-house employees included in the mandatory tip pool, as this was more fair and equitable, as back-of-house employees contributed to customer experience and directly impacted tips left by the customers.

43. Management revised the mandatory tip pool to include back-of-house employees, including the non-management cooks and dishwashers. When this change occurred, management did not reduce the back-of-house employees' wages. Since this change has occurred, management has continued to provide back-of-house employees with raises.

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44. Under this revised tip pool, approximately 1.5% (one and a half percent) of the tip pool goes to the back-of-house employees; the remainder of the tip pool continues to be paid out to the front-of-house employees.

45. This results in the back-of-house employees receiving, on average, approximately $1.25 per hour in tips from the tip pool, increasing their total hourly income to the following (on average): line cook – $13.75 per hour; prep cook – $11.25 per hour; and dishwasher – $10.25 per hour.

46. By way of comparison, the following positions receive the following average amounts in tips from the tip pool: servers and bartenders: $20.00 per hour (bringing their average hourly income to $28.80 per hour), bussers: $10.00 per hour (bringing their average hourly income to $18.80 per hour), hosts: $4.00 per hour (bringing their average hourly income to $14.00 per hour).

47. Since including back-of-house employees in the tip pool, Davis Street Tavern management and Ms. Ponton have noticed a greater level of camaraderie between the front-of-house employees and the back-of-house employees, a lower income disparity between the front-of-house and back-of-house employees, a higher level of morale and pride in work by the back-of-house employees, and an overall higher level of guest service and guest satisfaction.

48. Plaintiff Ponton has worked in other restaurants. In her experience, typically there is a divide between the front-of-house and back-of-house employees. This can be described as a form of a class distinction between the two groups, due to the great disparity in pay that results in all of the tips being kept among the front-of-house employees. This divide impacts team work among the groups of employees, and typically creates a friction in the restaurant. At Davis Street Tavern, since including the back-of-house employees in the tip pool, Plaintiff Ponton has noticed that this distinction between

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the front-of-house and back-of-house is no longer present, and there is a much higher amount of camaraderie, teamwork and respect among the employees.

49. Given these benefits, and in reliance on *Woody Woo*, Plaintiff Davis Street Tavern has continued its mandatory tip pool program that includes back-of-house employees. All new employees hired by Davis Street Tavern are made aware of their mandatory tip pool and that participation is a condition of employment.

50. The owners of Davis Street Tavern recently opened another restaurant in Portland Oregon. It is their preference to model the new location's tip pool on the one in place at Davis Street Tavern—in other words, having a mandatory tip pool that includes back-of-house employees in compliance with the Ninth Circuit's decision in *Woody Woo*.

STATUTORY FRAMEWORK

51. The FLSA establishes a minimum wage, requires overtime pay in certain circumstances, establishes child labor standards, and governs wage-related recordkeeping. 29 U.S.C. §§ 206, 207, 211, and 212. The FLSA does not regulate employment standards or compensation outside of these four areas.

52. Section 3 of the FLSA, 29 U.S.C. § 203, is the "definitions" section of the statute. A subpart, section 203(m), defines the term "wage." In doing so, section 3(m) allows employers to take a credit against the federal minimum wage for tips earned by employees (commonly referred to as the "tip credit"), provided certain conditions are met.

53. Per section 3(m), one such condition to taking the tip credit is that the employer must allow tipped employees to retain their tips, although the employer can require "the

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pooling of tips among employees who customarily and regularly receive tips." The relevant portion of section 3(m) states that:

> **The preceding 2 sentences [setting forth the tip credit] shall not apply with respect to any tipped employee unless such employee has been informed by the employer of the provisions of this subsection, and all tips received by such employee have been retained by the employee, except that this subsection shall not be construed to prohibit the pooling of tips among employees who customarily and regularly receive tips.**

29 U.S.C. § 203(m) (emphasis added).

54. The above statutory language has been in existence, largely unchanged, since 1974 and is the only provision in the FLSA that addresses tip pools.

THE *WOODY WOO* DECISION

55. In 2010, the Ninth Circuit Court of Appeals issued its ruling in *Cumbie v. Woody Woo, Inc.* 596 F.3d 577 (9th Cir. 2010).

56. With respect to the ownership of tips, the Ninth Circuit ruled that:

a. "Section 203(m) . . . does not alter the default rule in *Williams* [*v. Jacksonville Terminal Co.*, 315 U.S. 386, 397 (1942)] that tips belong to the servers to whom they are given only 'in the absence of an explicit contrary understanding' that is not otherwise prohibited." 596 F.3d at 582.

b. "Whether a server owns her tips depends on whether there existed an agreement to redistribute her tips that was not barred by the FLSA." *Id.*

c. "Such an agreement exist[s] by virtue of the tip-pooling arrangement [implemented by the employer]." *Id.*

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d. "Only the tips redistributed to [the server] from the pool ever belonged to her, and her contributions to the pool did not, and could not, reduce her wages below the statutory minimum." *Id.*

57. With respect to the applicability of federal tip pooling laws to employers who *do not take a tip credit*, the *Woody Woo* court ruled:

a. "The plain text of the third sentence [of Section 3(m)] . . . imposes *conditions* on taking a tip credit and does not state freestanding *requirements* pertaining to all tipped employees." *Id* at 581 (emphasis in original); and

b. Given "the plain language of the statute," and the "[a]bsen[ce] [of] an ambiguity," the court refused to "'alter the text [of Section 3(m)] in order to satisfy the policy preferences' of Cumbie and [the Department of Labor]." *Id.* at 582-583.

DOL ISSUED ITS FLAWED 2011 REGULATIONS

I. DOL Issued the 2011 Regulations In Direct Contravention of the FLSA's Clear Statutory Language and the Ninth Circuit *Woody Woo* Decision.

58. DOL's 2011 Regulations amended 29 C.F.R. §§ 531.52, 531.54, and 521.59 in a manner that is in direct contravention to the Ninth Circuit's *Woody Woo* decision. Indeed, this was DOL's declared intention.

59. The 2011 Regulations amended 29 C.F.R. § 531.52 by, among other things, replacing this language:

> In the absence of an agreement to the contrary between the recipient and a third party, a tip becomes the property of the person in recognition of whose service it is presented by the customer.

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with the following language:

> Tips are the property of the employee whether or not the employer has taken a tip credit under section 3(m) of the FLSA. The employer is prohibited from using an employee's tips, whether or not it has taken a tip credit, for any reason other than that which is statutorily permitted in section 3(m): As a credit against its minimum wage obligations to the employee, or in furtherance of a valid tip pool.

Compare 32 Fed. Reg. 13575, 13580 (Sept. 28, 1967), with current version of 29 C.F.R. § 531.52. *See also 2011 Regulations*, 76 Fed. Reg. at 18855.

60. The 2011 Regulations amended 29 C.F.R. § 531.54 by adding:

> **valid mandatory tip pools . . . can only include those employees who customarily and regularly receive tips**. However, an employer must notify its employees of any required tip pool contribution amount, may only take a tip credit for the amount of tips each employee ultimately receives, **and may not retain any of the employees' tips for any other purpose**.

29 C.F.R. 531.54 (emphasis added). *Compare* 32 Fed. Reg. 13575, 13580 (Sept. 28, 1967), with current version of 29 C.F.R. § 531.54. *See also 2011 Regulations*, 76 Fed. Reg. at 18856. Only the bold language is at issue in this action.

61. The 2011 Regulations amended 29 C.F.R. § 531.59 more extensively, many of which changes are not at issue in this action. The amendment relevant to this action involved replacing this sentence:

> Under employment agreements requiring tips to be turned over or credited to the employer to be treated by him as part of his gross receipts, it is clear from the legislative history that the employer must pay the employee the full minimum hourly wage, since for all practical purposes the employee is not receiving tip income.

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with the following sentence:

> With the exception of tips contributed to a valid tip pool as described in § 531.54, the tip credit provisions of section 3(m) also require employers to permit employees to retain all tips received by the employee.

Compare 32 Fed. Reg. 13575, 13581 (Sept. 28, 1967), with current version of 29 C.F.R. § 531.59. *See also 2011 Regulations*, 76 Fed. Reg. at 18856.

62. DOL's publication of the 2011 Regulations constitutes final agency action.

63. In publishing the 2011 Regulations, DOL did not deny that the Ninth Circuit ruled on the plain meaning of Section 203(m), or that the 2011 Regulations contradict the *Woody Woo* decision.

64. To the contrary, Defendants explained that "the Department respectfully believes that *Woody Woo* was incorrectly decided" and that "[t]he Ninth Circuit's 'plain meaning' construction is unsupportable." *2011 Regulations,* 76 Fed. Reg. at 18841-42 (citations omitted).

65. "A court's prior judicial construction of a statute trumps an agency construction otherwise entitled to Chevron deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion." *Irigoyen-Briones v. Holder*, 644 F.3d 943, 947, 949 (9th Cir. 2012) (finding statute was not ambiguous and, therefore, agency interpretation should not be given deference).

66. Defendants have admitted that the Ninth Circuit determined the plain meaning of section 3(m) in *Woody Woo*.

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67. Defendants cannot avoid the effects of *Woody Woo*, or otherwise ignore the clear meaning of section 3(m), simply by disagreeing with the Ninth Circuit.

II. Defendants Exceeded Their Authority in Issuing the 2011 Regulations.

68. Defendants can act only pursuant to a congressional grant of authority.

69. Section 3(m) does not grant Defendants authority to interpret or otherwise implement that Section's tip credit provision.

70. Within section 3(m), Congress granted Defendants authority to address specific aspects of wages, by stating:

> 'Wage' paid to any employee includes the reasonable cost, **as determined by the Administrator**, to the employer of furnishing such employee with board, lodging, or other facilities. . . . **Provided further, that the Secretary is authorized to determine the fair value of such board, lodging, or other facilities for defined classes of employees and in defined areas** . . ."

29 U.S.C. § 203(m) (emphasis added).

71. By way of contrast, section 3(m) does not have a similar grant of authority to Defendants to interpret its tip credit provision.

72. Defendants' authority under the FLSA is limited to enforcing minimum wage, overtime, child labor and recordkeeping requirements. Employment and compensation standards that fall outside these areas are outside the authority of Defendants to address.

73. Defendants have stated that "the Department only has authority under the FLSA to enforce, *inter alia*, the minimum wage provisions of the Act." *2011 Final Rule*, 76 Fed. Reg. at 18842 (citing 29 U.S.C. §§ 216, 217)

74. Defendants have admitted that the Secretary's ability to enforce section 3(m) is limited to instances where violations result in minimum wage or overtime violations.

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75. Defendants take the position that tips are not wages for purposes of the FLSA, except to the extent the employer takes a tip credit. *See, e.g.*, 29 C.F.R. § 531.60 ("Any tips received by the employee in excess of the tip credit need not be included in the regular rate. Such tips are not payments made by the employer to the employee as remuneration for employment within the meaning of the Act.").

76. Defendants' express reason for enacting the relevant 2011 Regulations was "to make clear that tips are the property of the employee, and that section 3(m) sets forth the only permitted uses of an employee's tips—either through a tip credit or a valid tip pool—whether or not the employer has elected the tip credit." *Final Rule*, 76 Fed. Reg. at 18842.

77. Declaring property rights in tips exceeds Defendants' authority under the FLSA.

78. Restricting the use of tips when the employer does not take a tip credit exceeds Defendants' authority under the FLSA.

79. Any attempt by Defendants to enforce the 2011 Regulations against an employer that does not take a tip credit is beyond Defendants' scope of authority under the FLSA.

III. DOL's 2011 Regulations Were Issued Without the Proper Notice and Comment Rulemaking Process

80. On July 28, 2008, DOL published the NPRM, explaining that it was revising a number of FLSA regulations to bring them up to date with amendments to the FLSA and court decisions interpreting the FLSA. *2008 NPRM*, 73 Fed. Reg. at 43656.

81. It is this 2008 NPRM that DOL relies upon for providing the public with notice of, and the ability to comment on, the 2011 Regulations.

82. The 2008 NPRM did not, however, put the public on notice that DOL was going to declare an absolute property right in tips such that section 3(m)'s limit on tip pools would

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apply even to employers who do not take a tip credit and who pay their employees at least the federal minimum wage.

83. In the 2008 NPRM, in discussing the changes to the regulations regarding the tip credit, DOL explained as follows concerning its understanding of section 3(m):

> Section 3(m) of the FLSA defines the term "wage" and **includes conditions for taking tip credits** when making wage payments to qualifying tipped employees under the FLSA. . . . Section 13(e) of the Fair Labor Standards Act Amendments of 1974 amended the last sentence of section 3(m) by providing that an employer **could not take a tip credit unless**. . . (2) all tips received by such employee have been retained by the employee, except that this subsection shall not be construed to prohibit the pooling of tips among employees who customarily and regularly receive tips.

2008 NPRM, 73 FR at 43659 (emphasis added).

84. In further discussing the tip credit provision of section 3(m), DOL explained,

> Section 3(m) provides the only method by which an employer may use tips received by an employee **to satisfy the employer's minimum wage obligation**. An employer's only options under section 3(m) are to take a credit against the employee's tips of up to the statutory differential, or to pay the entire minimum wage directly.
>
> The proposed rule updates the regulations to. . .**clarify that the availability of the tip credit provided by section 3(m)** requires that all tips received must be paid out to tipped employees in accordance with the 1974 amendments.

2008 NPRM, 73 FR at 43659 - 43660 (emphasis added).

85. Per the above, in the 2008 NPRM, DOL was putting the public on notice that it interpreted section 3(m) as placing a condition on an employer's use of the tip credit and that it intended to update the relevant regulations to clarify that employers could not use employees' tips to pay an employees' minimum wage in excess of the federal tip credit limit.

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86. This is far different from asserting an absolute property right in tips, or from stating that federal tip pool laws apply even when an employer pays its employees full minimum wage and does not take a tip credit.

87. The changes between the 2008 NPRM and the 2011 Regulations were so substantively different that interested parties reasonably could not have anticipated the final rulemaking found in the 2011 Regulations from the 2008 draft rules.

88. DOL therefore was required to provide new notice to the public of its intent to rule on these issues, to give the public the opportunity to meaningfully comment on them and to offer criticisms about them which DOL might find convincing.

89. By not being given notice in 2008 of DOL's intent to declare an absolute property right in tips and to rule that federal tip pooling laws apply even to employers who pay employees full minimum wage and do not take a tip credit, interested parties, including the Plaintiff Associations and their members, Davis Street Tavern, similar restaurants, and affected employees were never offered the opportunity to meaningfully comment on these issues and now are substantially harmed by DOL's publication and intent to enforce its 2011 Regulations.

IV. The 2011 Regulations are Arbitrary, Capricious and an Abuse of DOL Discretion

90. In publishing the 2011 Regulations, DOL explained that it was updating the regulations concerning tipped employees "to incorporate the 1974 amendments [to the FLSA], the legislative history, subsequent court decisions and the Department's interpretations." 76 Fed. Reg. 1at 18839. DOL further stated that "Congress deliberately amended the FLSA's tip credit provisions in 1974 to clarify that section 3(m) provides the only permitted use of an

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employee's tips – through a tip credit or a valid tip pool among only those employees who customarily and regularly receive tips." *Id.* at 18841.

91. However, upon information and belief, DOL failed to consider an important part of the relevant legislative history, in which Congress made clear its intent that employers could lawfully mandate tip pools and tip sharing agreements that included employees who do not customarily and regularly receive tips, and that such employers would simply lose the benefit of the tip credit in such instances.

92. By failing to consider this component of the relevant legislative history, DOL acted arbitrarily and capriciously.

93. In publishing the 2011 Regulations, DOL also stated that it "has determined that the final rule changes will not result in any additional compliance costs for regulated entities because the current compliance obligations derive from current law and not the outdated regulatory provisions that have been superseded years ago." 76 Fed. Reg. at 18851. DOL published this determination in lieu of conducting an assessment of the negative impact of the 2011 Regulations on small businesses as is required by the Regulatory Flexibility Act, 5 U.S.C. § 601, *et seq.* ("RFA").

94. DOL's determination is unfounded, not based on any factual analysis and based on an inaccurate premise.

95. DOL's determination that the 2011 Regulations will not result in additional compliance costs is based on its premise that "the current compliance obligations derive from current law and not the outdated regulatory provisions that have been superseded years ago."

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96. The pertinent portions of the 2011 Regulations, however, did not "derive from current law"; they completely were at odds with the law in effect at that time (and still in effect), as set forth by the *Woody Woo* decision.

97. A factual analysis will show that the 2011 Regulations will result in additional compliance costs to businesses, and the impact on small businesses will be substantial.

98. A substantial number of full-service restaurants are considered small businesses, as defined by the U.S. Small Business Administration, with annual sales under $7 million. *2007 Economic Census*, U.S. Bureau of the Census (the "2007 U.S. Economic Census"). Forty-six percent (46%) of all full-service restaurants have under $500,000 in gross annual income. *2007 U.S. Economic Census.* Eighty-five percent (85%) of all full-service restaurants have fewer than 50 employees. *2007 U.S. Economic Census.*

99. As set forth previously, and incorporated herein by reference, the 2011 Regulations will, if not invalidated by this Court, result in substantial "additional compliance costs for regulated entities," and will, if not invalidated, have a substantial negative impact on small businesses. These costs include lower morale and turnover by individuals removed from the tip pool, having to increase the wages of the employees who are taken out of the tip pool, to supplement their loss of tips or, if businesses choose not to comply with the 2011 Regulations, they will face costs associated with defending that action if they become the target of a private lawsuit or DOL enforcement action.

100. In publishing the 2011 Regulations, DOL also stated that it "has determined that this rule . . . does not involve implementation of a policy. . . that could impose limitations on private property use." 76 Fed. Reg. at 18854.

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101. The 2011 Regulations do impose limits on private property in several ways.

102. For example, DOL's 2011 Regulations declare a property right in tips, and then prohibit employees who allegedly own those tips to enter into agreements with their employer to share the tips with certain other employees, even if such tipped employees desire to do so.

103. Moreover, DOL takes the enforcement position that "employees who customarily and regularly receive tips" includes "waiters, waitresses, bellhops, counter personnel (who serve customers), bussers, and service bartenders" but *does not include* "dishwashers, cooks, chefs, and janitors." *DOL Fact Sheet Number 15.* DOL takes the position that, as a result, dishwashers, cooks, chefs and expeditors are prohibited from being included in mandatory tip pools.

104. By doing this and trying to make unlawful the types of tip pooling arrangements expressly declared lawful by the *Woody Woo* decision, DOL is stripping back-of-house employees of their current right to a share in tips left by customers. In other words, DOL is declaring a property right in tips, and then taking that property from back-of-house employees who, in accordance with *Woody Woo*, have been able to share in them (assuming the employer pays the employees at least full minimum wage and does not take a tip credit).

105. Thus, DOL's 2011 Regulations are arbitrary, capricious, an abuse of discretion, and contrary to the law.

CLAIMS FOR RELIEF

COUNT I
(Violation of APA: Exceeded Statutory Authority)

106. Plaintiffs re-state and incorporate by reference the preceding paragraphs as if fully set forth herein.

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107. Defendants' 2011 revisions to 29 CFR 531.52, 29 CFR 531.54 and 29 CFR 531.59 at issue in this lawsuit are not authorized under the FLSA or any other law.

108. Defendants' 2011 revisions to 29 CFR 531.52, 29 CFR 531.54 and 29 CFR 531.59 at issue in this lawsuit exceed Defendants' statutory jurisdiction and authority.

109. Accordingly, the 2011 revisions to 29 CFR 531.52, 29 CFR 531.54 and 29 CFR 531.59 at issue in this lawsuit are in excess of Defendants' statutory authority, jurisdiction, and limitations, in violation of 5 U.S.C. § 706(2)(C), and are not in accordance with law, in violation of 5 U.S.C. § 706(2)(A).

110. Because of Defendants' actions, Plaintiffs and Association Plaintiffs' members have suffered harm as set forth above, including a significant increase in their costs and substantial additional burden associated with complying with the 2011 Regulations, as well as exposure to legal claims for failure to comply with these new requirements. Moreover, Plaintiff Ponton has suffered harm, also as set forth above.

111. Plaintiffs have no other adequate remedy in court or administratively for Defendants' unlawful action as described herein, and such action has caused Plaintiffs to suffer undue and actual hardship and irreparable injury.

COUNT II
(Violation of APA: Abuse of Discretion and Not In Accordance with the Law)

112. Plaintiffs re-state and incorporate by reference the preceding paragraphs as if fully set forth herein.

113. Under the APA, a reviewing court must set aside an agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 5 U.S.C. § 706(2)(A).

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114. Defendants promulgated the 2011 Regulations in violation of the APA as they are an abuse of discretion and otherwise not in accordance with the law.

115. Section 3(m) imposes *conditions* on taking a tip credit and does not state freestanding *requirements* pertaining to all tipped employees.

116. This is clear from section 3(m)'s plain language. This is also consistent with DOL's own interpretation of section 3(m) – for example, as stated in the 2008 NPRM.

117. The Ninth Circuit's 2010 *Woody Woo* decision also determined the plain meaning of section 3(m).

118. Similarly, the Ninth Circuit's *Woody Woo* decision set forth the law with respect to the ownership of tips.

119. Defendants' 2011 revisions to 29 CFR 531.52, 29 CFR 531.54 and 29 CFR 531.59 at issue in this lawsuit are directly contrary to, and inconsistent with, *Woody Woo* and the plain meaning of section 3(m) as declared by the Ninth Circuit.

120. Therefore, Defendants' 2011 revisions to 29 CFR 531.52, 29 CFR 531.54 and 29 CFR 531.59 at issue in this lawsuit are not entitled to deference, are arbitrary and capricious, are an abuse of discretion and contrary to the law. *Irigoyen-Briones v. Holder*, 644 F.3d 943, 947, 949 (9th Cir. 2012).

121. Because of Defendants' actions, Plaintiffs and Association Plaintiffs' members have suffered harm as set forth above, including a significant increase in their costs and substantial additional burden associated with complying with the 2011 Regulations, as well as exposure to legal claims for failure to comply with these new requirements. Moreover, Plaintiff Ponton has suffered harm, also as set forth above.

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122. Plaintiffs have no other adequate remedy in court or administratively for Defendants' unlawful action as described herein, and such action has caused Plaintiffs to suffer undue and actual hardship and irreparable injury.

COUNT III
(Violation of APA: Arbitrary and Capricious)

123. Plaintiffs re-state and incorporate by reference the preceding paragraphs as if fully set forth herein.

124. Defendants promulgated the 2011 Regulations in violation of the APA as they are arbitrary and capricious.

125. In promulgating the 2011 Regulations, Defendants failed to consider relevant legislative history concerning the 1974 amendments to the FLSA, in which Congress made clear their intention that section 3(m) was not intended to prohibit mandatory tip pools that include employees who do not customarily and regularly receive tips; instead, Congress intended only for employers in such instances to not be eligible for the tip credit.

126. As further evidence of Defendants' arbitrary and capricious actions in promulgating the 2011 Regulations in violation of the APA, Defendants failed to assess the negative impact of the 2011 Regulations on small businesses as required under the APA and the RFA. Instead of conducting such an analysis, Defendants made a determination that the 2011 Regulations would not have a negative financial impact on such businesses. That determination, however, was specious, not supported by any facts, and based on the inaccurate premise that the 2011 Regulations were "derived from current law," notwithstanding the *Woody Woo* decision.

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127. Additional evidence of Defendants' arbitrary and capricious actions in promulgating the 2011 Regulations is Defendants' statement that the Regulations would not "impose limitations on private property use." This is notwithstanding the fact that the very essence of the Regulations is to impose limits on private property use, by declaring property rights in tips, and then prohibiting certain contracts and agreements regarding those tips, and depriving current holders of such property from continuing to receive it.

128. Therefore, Defendants' 2011 revisions to 29 CFR 531.52, 29 CFR 531.54 and 29 CFR 531.59 at issue in this lawsuit are not entitled to deference, are arbitrary and capricious, are an abuse of discretion and contrary to the law.

129. Because of Defendants' actions, Plaintiffs and Association Plaintiffs' members have suffered harm as set forth above, including a significant increase in their costs and substantial additional burden associated with complying with the 2011 Regulations, as well as exposure to legal claims for failure to comply with these new requirements. Moreover, Plaintiff Ponton has suffered harm, also as set forth above.

130. Plaintiffs have no other adequate remedy in court or administratively for Defendants' unlawful action as described herein, and such action has caused Plaintiffs to suffer undue and actual hardship and irreparable injury.

COUNT IV
(Violation of APA: Denial Of Notice And Comment Rights)

131. Plaintiffs re-state and incorporate by reference the preceding paragraphs as if fully set forth herein.

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132. Under the APA, an "agency shall give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments with our without opportunity for oral presentation." 5 U.S.C. § 553.

133. This requirement prohibits an agency from adopting final rules that differ from its proposed rules "when the changes are so major that the original notice did not adequately frame the subjects for discussion." *Connecticut Light and Power Co. v. Nuclear Regulatory Comm'n*, 673 F.2d 525, 533 (D.C. Cir.).

134. A court must "hold unlawful and set aside agency action, findings, and conclusions found to be. . .without observance of procedure required by law." 5 U.S.C. § 706(2)D).

135. The 2011 Regulation provisions at issue in this case depart substantially from the proposed regulations noticed by DOL in its 2008 NPRM. The 2011 Regulations are a major and material change from the 2008 NPRM, such that the 2008 original notice did not adequately frame the 2011 Regulations as a subject for discussion.

136. Interested parties could not reasonably have anticipated from the 2008 NPRM that Defendants would ultimately declare absolute property rights in tips such that section 3(m)'s limit on tip pools would apply even to employers who do not take a tip credit and who pay their employees at least the federal minimum wage.

137. DOL therefore was required to provide new notice to the public of its intent to rule on these issues, to give the public the opportunity to meaningfully comment on them and to offer criticisms about them which DOL might find convincing.

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138. Accordingly, Defendants violated the APA by issuing the 2011 revisions to 29 CFR 531.52, 29 CFR 531.54 and 29 CFR 531.59 at issue in this lawsuit without observance of the procedures required by law.

139. The Plaintiff Associations, their members, Davis Street Tavern, and their employees, including Plaintiff Ponton, lacked sufficient notice of, and were therefore unable to comment upon, those aspects of the 2011 Regulations before they became final.

140. Because of Defendants' actions, Plaintiffs and Association Plaintiffs' members have suffered harm as they were not permitted the opportunity to comment on the new tip notice requirements before they became final, as required by the APA, resulting in significant increase in their costs, substantial additional burden, and exposure to legal claims for failure to comply with these new requirements. Moreover, Plaintiff Ponton has suffered harm, also as set forth above.

141. Plaintiffs have no other adequate remedy in court or administratively for Defendants' unlawful action as described herein, and such action has caused Plaintiffs to suffer undue and actual hardship and irreparable injury.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs pray that this Court:

1. Declare the provisions of the 2011 Regulations revising 29 C.F.R. 531.52, 29 C.F.R. 531.54 and 29 C.F.R 531.59 outlined and described herein unlawful, void, and unenforceable.

2. Vacate and set aside the provisions of the 2011 Regulations revising 29 C.F.R. 531.52, 29 C.F.R. 531.54 and 29 C.F.R. 531.59 outlined and described herein.

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3. Immediately issue a Preliminary Injunction enjoining the Defendants, their officers, agents, employees and all other persons acting in concert with them, from acting in any manner to enforce or otherwise act under the authority of the provisions of the 2011 Revisions to 29 C.F.R. 531.52, 29 C.F.R. 531.54 and 29 C.F.R. 531.59 outlined and described herein.

4. Issue all process necessary and appropriate to enjoin Defendants and their officers, employees, and agents from implementing, applying, enforcing or taking any action whatsoever pursuant to the provisions of the 2011 Regulations revising 29 C.F.R. 531.52, 29 C.F.R. 531.54, and 29 C.F.R. 531.59 outlined and described herein, pending the conclusion of this case and, as appropriate, thereafter.

5. Declare that any action taken by Defendants pursuant to the provisions of the 2011 Regulations revising 29 C.F.R. 531.52, 29 C.F.R. 531.54, and 29 C.F.R. 531.59 outlined and described herein is null and void and contrary to law.

6. Award Plaintiffs costs and reasonable attorneys' fees as appropriate.

7. Grant such further and other relief as this Court deems just and proper.

8. Permit Plaintiffs' pleadings to conform to the proofs.

DATED this 12th day of July, 2012.

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