

## MEMORANDUM

**From:** Jasmine Adams

**Date:** April 19, 2022

**Re:** Decreasing the incidence of wage theft among tipped workers

---

### Issue Summary

Approximately 17 percent of low wage workers lose a quarter of their income to employer wage theft in the form of minimum wage violations each year.<sup>1</sup> The theft rate is highest in the service industry where consumer tips are expected to subsidize the growing difference between the tipped federal minimum wage (\$2.13) and the nontipped federal minimum wage (\$7.25). Over 1 in 10 U.S. workers are employed in the leisure and hospitality sector, wherein nearly half of tipped workers rely on public benefits.<sup>2</sup> These workers are also twice as likely to live in poverty compared to nontipped workers.<sup>2</sup> Government action is needed to combat the rising economic inequality perpetuated by employer malpractice in tip-subsidized industries.

### Policy Options

To limit the incidence of wage theft among low wage, tipped workers, policymakers may consider implementing the following reforms:

**1. End forced arbitration and limits on collective bargaining in the wage dispute process.**

Companies that force employees to settle wage disputes through private arbitration as a contingency of employment put their employees at an increased risk for retaliation, mandated nondisclosure agreements, and uneven bargaining power in the wage dispute process. To increase the viable avenues through which tipped workers may dispute wage theft claims and recover lost wages, Congress may enact legislation that voids mandated arbitration clauses for all claimants of workplace misconduct.

**2. Close policy loopholes in subcontracting, franchising, and minimum wage exemptions.**

Companies that adopt decentralizing business strategies often conduct minimum wage violations through employment misclassification, outsourced management, and unpaid internships. Congress may decrease the scope of limited liability protections to hold parent companies accountable for their misuse of independent contracting and subminimum wage labor.

**3. Require employers to pay the nontipped federal minimum wage.**

Food delivery and home cleaning are just a couple of the industries that are systemically prone to minimum wage theft due to their demand for largely independent work which takes place in informal or unregulated domains. Congress may follow the footsteps of “One Fair Wage” states and remove structural incentives to wage theft by requiring employers to directly payout sufficient wages.

---

<sup>1</sup> Cooper, David., and Kroeger, Teresa. (2017). Employers steal billions from workers’ paychecks each year. Economic Policy Institute.

<sup>2</sup> Allegretto, Sylvia A., and Cooper, David. (2014). Twenty-Three Years and Still Waiting for Change. Economic Policy Institute.

## Evidence

At least 98% of workers experiencing workplace violations opt to abandon or forgo pursuing a claim when claims are subject to employer-mandated arbitration.<sup>3</sup> Companies that forbid workers from filing group claims further discourage employees by requiring that they file independent claims for widespread wage violations that are burdensome to pursue alone. Protecting workers' right to dispute violations in court would expand employee bargaining power by ensuring greater transparency and objectivity in the wage dispute process. Given that 80% of nonunion private-sector companies are projected to include arbitration and limited collective bargaining clauses in their employee contracts by 2024,<sup>3</sup> it is imperative to provide the most vulnerable workers with a fair and viable avenue for disputing minimum wage violations. Nonetheless, state governments' capacity to process and follow up on wage theft claims ranges from moderate to nonexistent. Likewise, the Department of Labor fails to track down a substantial portion of stolen wages even after claims have been won. Considering these limitations, ending forced arbitration and limited collective bargaining would not meaningfully reduce wage theft among tipped service workers.

Businesses are increasingly using decentralizing business strategies to subvert their fiscal responsibilities to their employees. An estimated 10 to 20 percent of the U.S. workforce is misclassified as independent contractors and thus artificially exempt from receiving compensation equal to at least the federal minimum wage.<sup>4</sup> Likewise, franchised outlets have far higher levels of noncompliance with federal minimum wage requirements than company-owned establishments.<sup>5</sup> Compounding these issues are federal exemptions that permit employers to pay workers under 20 years old less than the federal minimum wage for up to 3 months of full-time work.<sup>6</sup> Allowing the government to hold employers accountable for exploiting labor market loopholes would deter employers from committing systemic wage theft among a sizable portion of the tipped labor market. Nevertheless, plans to expand corporate liabilities would undoubtedly trigger significant pushback from corporate interest groups and could produce unintended negative externalities for legitimate businesses and independent contractors.

Wage and hour practices unique to the service industry such as tip sharing, irregular scheduling, and nontipped work hours make it virtually impossible for tipped workers to assess whether they've received sufficient pay with any true precision. Immigrants, young people, women, and people of color are overrepresented among tipped workers and are the most likely to receive lower tips due to customer discrimination. Requiring employers to pay tipped workers a universal living wage rather than the tipped minimum wage would help rectify this variance and allow workers to identify and dispute wage violations more concretely. This approach would nonetheless transfer the wage burden to the consumer via higher prices.

## Recommendation

Despite concerns that replacing the dual minimum wage with a universal living wage would hinder employment and economic growth, studies find that business growth in "One Fair Wage" states outpaces industry growth in dual wage states, with tipped workers receiving about 14.2 percent more in earnings compared to tipped workers in other states.<sup>7</sup> Congress should enhance transparency, equity, and employer accountability in service sector compensation by replacing the tipped minimum wage with a universally applicable fair minimum wage.

---

<sup>3</sup> Baran, Hugh. (2021). Forced Arbitration Helped Employers Who Committed Wage Theft Pocket \$9.2 Billion in 2019 From Workers in Low-Paid Jobs. *National Employment Law Project*.

<sup>4</sup> Carré, Françoise. (2015). (In)dependent Contractor Misclassification. *Economic Policy Institute*.

<sup>5</sup> Ji, M., & Weil, D. (2015). The Impact of Franchising on Labor Standards Compliance. *ILR Review*.

<sup>6</sup> U.S. Department of Labor. Subminimum Wage. <https://www.dol.gov/general/topic/wages/subminimumwage>.

<sup>7</sup> Allegretto, Sylvia A., and Cooper, David. (2014). Twenty-Three Years and Still Waiting for Change.