Tip of the iceberg: Tip skimming is an underreported problem

Class actions may arise out of management skimming off all or part of tips left for service employees

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Tip skimming (when restaurant owners and managers take tips that belong to their employees) is an underreported problem. A recent Seattle survey of restaurant staff found just six percent complained about tip skimming. (http://www.thestranger.com/food-and-drink/feature/2015/11/18/23160220/do-you-know-where-your-tip-goes.) However, a similar survey of sexual harassment among restaurant workers found reported rates of 15 percent that increased to 90 percent when more specific questions were presented. (*Ibid*.) It is also difficult to measure the extent of this problem, because many patrons leave cash tips that may not be documented. (See http://thetruthaboutbartending.com/2012/01/26/bar-manager-theft/.) But based on the relatively high number of tip skimming claims against well-known restaurants and the scope of published settlements, the problem appears to be substantial and pervasive.

Why would tip skimming be underreported? Because many workers live paycheck-to-paycheck, and they worry about (unlawful) retaliation. The median hourly pay for foodservice employees is about 17 percent less than what workers earn in comparable industries. (http://www.huffingtonpost.com/saru-jayaraman/a-bittersweet-day-for-wor_b_9858140.html.)

Why should anyone but tipped employees care about tip skimming? Because many restaurant workers rely on public assistance which is financed through taxes (See http://www.epi.org/publication/restaurant-workers/). Restaurant owners who skim tips are essentially socializing their costs of doing business and concealing the actual cost of dining out. (*Ibid*.)

Tip skimming also creates an incentive for employees to work when they are sick because, without their full tips, restaurant workers cannot afford to stay home, unpaid. This increases the risk of illness transmitted from restaurant employees to their customers. (https://www.dol.gov/featured/paidleave/get-the-facts-sicktime.pdf.) (As of 2014 with the passage of AB1522, restaurant workers now can earn up to just three paid sick days per year.)

Tip skimming presents an opportunity for attorneys to help tipped workers seek justice. This article discusses tip-related liability to help you evaluate potential tip skimming claims and address them with available remedies.

Lawful tip "pooling" and unlawful tip skimming

• ***What is a tip?***

A "tip" or "gratuity" is usually money that a customer has given to an employee, over and above the actual amount due for services rendered. (Lab. Code, § 350.) Under Labor Code, section 351, employers cannot take or receive any part of a gratuity. (See *Leighton v. Old Heidelberg, Ltd.* (1990) 219 Cal.App.3d 1062, 1068 ["*Leighton*"]; *Herbert's Laurel-Ventura, Inc. v. Laurel Ventura Holding Corp.* (1943) 58 Cal.App.2d 684, 694 ["A tip is not intended for the proprietor of restaurant"].)

• ***What is tip "pooling?"***

Generally, tip pooling occurs when a restaurant (or another business with tipped staff) requires employees who receive tips directly to contribute a portion of those tips to others who provide customer service. (See *Leighton* at *p.* 1067.) These include workers like busboys, bartenders, and servers. (*Leighton* at p. 1066.)

The key factors in determining the propriety of a tip pool are that (1) the employees in the tip pool are "in the chain of service bargained for by the patron, pursuant to industry custom," and (2) the pooled tips are distributed pro-rata, *i.e.*, "based on the number of hours they worked, as is consistent with industry custom." (2005 Cal. DLSE LEXIS 1, *4-*5.)

Tip pooling is allowed under California Labor Code, section 351, even if involuntary (as long as owners and managers do not share in tips, even if they are in the chain of service). A cause of action generally will not lie for conversion or the common count of money had and received, because a gratuity left with wait-staff "belonged to" other employees in the first instance. (*Avidor v. Sutter's Place, Inc.* (2013) 212 Cal.App.4th 1439, 1452, 1455; see Lab. Code, § 351.)

Tip pooling can include all staff who contribute to a customer's service, even if they do not provide "direct table service." (*Etheridge v. Reins International California, Inc.* (2009) 172 Cal.App.4th 908, 922.) Labor Code section 351, does not define "direct" or "indirect" table service. Given the different types of restaurants and level of staffing, tip pooling requires a

flexible definition of persons who are entitled to share in the proceeds; a definition that restricted it to persons who provided direct service would be unworkable. (*Budrow v. Dave & Buster's of California, Inc.* (2009) 171 Cal.App.4th 875, 881 ["*Budrow*"].) For example, a bartender who mixes a drink directly for a specific person still provides a service for the customer, even if he or she does not directly serve or bill for the drink. (*Budrow* at pp. 881-882.)

The statute's reference to tips that have been provided to an employee or "employees," plural, contemplates that customers may have intended their gratuity for more than just one person. (See *Leighton* at p. 1069.) "The average diner has little or no idea and does not really care who benefits from the gratuity he leaves, as long as the employer does not pocket it, because he rewards for good service no matter which one of the employees directly servicing the table renders it." (*Leighton* at p. 1069.) "It is simply not possible to devise a system that works with mathematical precision and Solomonic justice in each one of the millions of transactions that take place every day." (*Budrow* at p. 882.)

• **Why pool tips?**

Tip pooling promotes efficient service and good relations among service employees. (*Leighton* at p. 1071.) "Tipping out is an acknowledgment of the truth of food service, which is that, from top to bottom, a restaurant staff is a team." (http://www.chowhound.com/food-news/108058/after-batali-bust-arguments-for-and-against-tipping-out/)

Tip pooling vs. unlawful tip skimming

Unlawful tip *skimming* occurs when employers or their agents participate in a tip pool or keep any portion of a tip that a customer leaves for non-management employees. (Lab. Code, § 351.)

Tip skimming is a pervasive problem

In 2012, celebrity chef Mario Batali and restauranteur Joe Bastianich paid $5.25 million to settle a tip skimming class action filed in U.S. District Court for the Southern District of New York. (http://dinersjournal.blogs.nytimes.com/2012/03/07/mario-batali-agrees-to-5-25-million-settlement-over-employee-tips/?ref=nyregion&_r=1) The defendants allegedly deducted about 4 to 5 percent of nightly wine sales from the tip pool and kept it for themselves. (*Ibid*.) They allegedly attempted to excuse their tip skimming by complaining that it covered some costs of doing business, like broken glassware. (*Ibid*.) However, at a staff meeting, an executive "refused to justify the policy and said it was not going to change." (*Ibid*.) Evidence supporting the unlawful tip skimming included a spreadsheet that allocated the tip pool. (*Ibid*.)

In 2014, a Philadelphia-area restaurant chain that allegedly skimmed tips paid over $8.5 million to settle claims filed on behalf of about 1,250 workers (an average of about $6,800 per employee). (http://www.metro.us/local/chickie-s-and-pete-s-will-pay-employees-6-8m-for-tip-skimming-scam/tmWnbt-926bTpkiyOASE/.) The defendant also allegedly required employees to buy their own vacuums to clean their work areas, even though restaurants must cover their own costs of doing business. (*Id.*; Lab. Code, § 2802.)

In fall 2015, a complaint was filed against Donald Trump in a New York state court that alleged the Trump Organization kept the 22 percent service charge added to catering costs at the Trump SoHo hotel. (https://www.dnainfo.com/new-york/20160307/soho/trump-soho-hotel-stiffed-caterers-out-of-tips-lawsuit-charges.) The complaint alleged that reasonable customers would have assumed that the charge was a gratuity for waitstaff, because the menu or bill did not clearly disclose that management kept some or all of the service charge (as required under New York law). (http://www.grubstreet.com/2016/03/donald-trump-sued-tips.html.)

Incorrect tip calculations happen even when automated systems are in place that purportedly calculate tips accurately for waitstaff. The Olive Garden recently implemented an automated ordering system using tablet computers. (http://finance.yahoo.com/news/olive-garden-servers-getting-shorted-162716202.html.) When some customers added a tip of, *e.g.*, 20 percent, the software calculated a tip of only about 15 percent. (*Ibid*.) The Olive Garden "moved immediately" to address this problem upon receiving notice of it. (*Ibid*.) While management apparently did not skim the missing five percent of the bill, it would probably not be difficult to make this happen.

Tip skimming also affects tipped workers beyond the restaurant business. In August 2015, an exotic dancer in Philadelphia filed a class-action claim alleging, inter alia, that managers took a percentage of her tips and required her to work off the clock. (http://www.phillymag.com/news/2015/08/25/delilahs-den-lawsuit-carlee-costello/.)

Employers must cover costs of doing business

An employer must cover the costs of doing business and cannot shift them to the employees. California employers cannot deduct the cost of credit card processing fees from tips left on credit cards. (Lab.Code, § 351.)

Tips cannot be credited against minimum wage

Although some states allow an employer to credit employee tips against the amount required to pay for the minimum wage, California proscribes this practice. (Lab. Code, § 351; *Leighton at p.* 1068.) California requires paying restaurant workers the same minimum wage as in other industries, and the legislature intended that only employees should benefit from customers' tips. (California Minimum Wage Order MW-2014; (*Henning v. Industrial Welfare Com.* (1988) 46 Cal.3d 1262, 1278 ["*Henning*"].)

Just as in other industries, restaurants cannot hire employees to work only for tips or contract to pay employees less than the minimum wage. (California Minimum Wage Order MW-2014; *Leighton* at p. 1068.)

Employer cannot share in employees' tips

In *Jameson*, a restaurant required servers to share 10 percent of their tips with a floor manager who had authority to hire and control employees. (*Jameson v. Five Feet Restaurant, Inc.* (2003) 107 Cal.App.4th 138, 141-142, 144 ["*Jameson*"].) Acknowledging that *Leighton* generally supported tip pooling for workers who served patrons, the *Jameson* court noted specifically that "an employer or agent" who hires, supervises, directs, or controls employees could not share any portion of an employee's tip. (*Jameson* at p. 141.) The court reasoned that under Labor Code, sections 350 and 351, the Legislature intended that only non-management employees had a right to receive tips, and there was no exception for managers who participated in serving customers. (*Jameson* at p. 144.)

But some supervisory employees can take tips

However, supervisors who spend most of their time performing entry-level work can share in tips provided collectively. In *Chau v. Starbucks Corp.*, the issue was whether "shift supervisors" who spent most of their time directly serving customers properly shared in tips that customers placed in a collective tip box. (*Chau v. Starbucks Corp.* (2009) 174 Cal.App.4th 688, 691 [modified and reh'g denied, 2009 Cal. App. LEXIS 1081].) Because (1) shift supervisors were hourly employees who spent most of their time performing the same customer service tasks as entry-level employees, (2) they did not have authority to hire or fire, (3) salaried store managers did not share in the tips, and (4) no authority prohibited a "service employee" from keeping a portion of a "*collective* tip," the employer's policy did not violate Labor Code, section351. (*Id*. at pp. 691, 692-693, 694-695 [emphasis added].)

Mandatory "service charge" vs. voluntary tipping

While a tip is a voluntary payment *over and above* the amount owed for a meal, a "service charge" is a mandatory cost that the customer must pay based on, *e.g.*, prior agreement or published on the menu. (http://www.dir.ca.gov/dlse/FAQ_TipsAndGratuities.htm.) Because these charges are due and owing, the employer is not obligated to share any or all of the proceeds with its employees. (http://www.dir.ca.gov/dlse/FAQ_TipsAndGratuities.htm.) However, if the charge is "is waivable or negotiable, or couched in terms of being less than a fixed amount which must be paid, the charge is not an added "charge" to the bill and payment is gratuitous." (DLSE Enforcement Policies and Interpretations Manual (March 2006) 19.3.5.) Potential clients who are concerned about tip skimming should determine whether their restaurant uses the terms "gratuity" and "service charge" interchangeably (preferably in writing), whether they (and other non-management staff) are receiving all of the tip proceeds, and if the purportedly mandatory service charges are negotiable.

Potential claims

• ***Unfair business practices: class-action claims cognizable for tip skimming***

There is no private right of action for tip skimming under Labor Code, section 351, but a cause of action will lie under Business and Professions Code section 17200. (*Lu v. Hawaiian Gardens Casino, Inc.* (2010) 50 Cal.4th 592, 600-601; *O'Connor v. Uber Techs., Inc.* (N.D.Cal. 2014) 58 F.Supp.3d 989, 1008.) A class-action complaint filed on behalf of California and Massachusetts Uber drivers alleged, inter alia, that the company skimmed tips. (*O'Connor v. Uber Techs., Inc.* (N.D. Cal. 2014) 3:13-cv-03826-EMC, Dkt. 330, ¶¶ 15-17.) Plaintiffs alleged that the company represented to customers that tips were included with their fares, but that the company kept at least a portion of those tips, in violation of Labor Code section 351. (*O'Connor v. Uber Techs., Inc.* (N.D. Cal. 2014) 3:13-cv-03826-EMC, Dkt. 330, ¶¶ 15-17.)

The O'Connor plaintiffs pleaded this claim as a violation of Business & Professions Code section 17200. (*Id*. at ¶ 34.) On April 21, 2016, the parties filed a motion for preliminary approval of a proposed $84 million-plus settlement that includes compensation for skimmed tips. (*O'Connor v. Uber Techs., Inc.* (N.D. Cal. 2014) 3:13-cv-03826-EMC, Dkt. 519-6, ¶ 102(a).) (N.b., as of the date of submitting this article, the lead plaintiff has now apparently expressed concerns with the terms of the settlement. http://www.law360.com/classaction/articles/796793?nl_pk=f777a7b6-a9e2-48e1-a9c5-5d4da88a75a6&utm_source=newsletter&utm_medium=email&utm_campaign=classaction.)

• **Criminal prosecution or conversion**

Tip skimming is a misdemeanor that is punishable by a fine of $1,000 or up to a 60-day sentence. (Lab. Code, § 354.) Potential clients may also consider a conversion claim for tip skimming.

Retaliation for adverse action following report of tip skimming

A cause of action for retaliation will likely lie against an employer who takes adverse employment action against an employee who complains about tip skimming. (See Lab. Code, § 98.6(a).) Although few retaliation claims make headlines, there is strength in numbers. In May 2013, about half of the waitstaff at a prominent Philadelphia sushi restaurant walked off the job to protest tip skimming. (www.grubstreet.com/2013/05/fat-salmon-workers-go-on-strike.html.) The restaurant owner allegedly retaliated against the complaining employees by reducing their hours. (*Ibid*.) The restaurant settled its tip skimming claims for an average of $8,000 per employee.

(www.newsworks.org/index.php/local/ philadelphia/62508-suit-over-skimmed-tips-at-philly-restaurant-ends-in-40000-settlement.)

Many food industry workers live on hard-earned tips. Tip-skimming class actions can help restaurant owners and managers learn there is no free lunch.

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