



**NOTICE OF INCLUDED GRATUITY
OR SERVICE CHARGE**

**House Bill 4657 (Substitute H-3)
First Analysis (3-19-02)**

**Sponsor: Rep. Glenn S. Anderson
Committee: Regulatory Reform**

THE APPARENT PROBLEM:

Leaving a tip for food service staff is an expected part of dining out for most people. Since tipped employees may be paid less than the minimum wage rate, many people willingly leave a tip for the server and other staff equaling between 15 and 20 percent of the cost of the meal. In fact, because tipping is so commonplace, the increasing practice of food service establishments to automatically include a gratuity or fee for service in a customer's bill has gone relatively unnoticed. Unfortunately, this practice has led to two problems. First, not all restaurants and other food service establishments are equally diligent about making certain that the customer is informed of the fact that an automatic gratuity has been included in his or her bill, and secondly, not all food service establishments pass all or even some of the alleged gratuity on to the staff, even though most patrons probably assume that all of the gratuity would go to the staff.

An example of the type of abuse of the gratuity or service charge was described as follows: An establishment was contracted with to provide food and drinks for a wedding reception. The bill included an 18 percent gratuity that amounted to \$1,683.90. Since nine servers worked for four hours each during the reception, that should have meant that each server would receive approximately \$187 from the gratuity. Instead, the caterer paid each of the servers \$40 and kept the remaining \$1,323.90 for itself.

In light of this practice of including automatic gratuities and the problems that have arisen, legislation has been introduced to require that restaurants and other food service establishments notify their customers of the amount of any automatic service charge or gratuity that they are being charged and how much of that amount will be retained by the establishment rather than be given to the staff.

THE CONTENT OF THE BILL:

House Bill 4657 would create an act to require that

patrons of food service establishments be given notice of any automatic gratuity or service charge that would be added to their bills. Specifically, a food service establishment that charged an automatic gratuity or service charge, or both, would have to include, at least, a notice indicating the amount charged, either as a fixed amount or as a percentage of the customer's bill. The notice would have to be printed upon each bill and upon either the menu or upon a poster placed conspicuously in the customer service area of the establishment. The notice would have to be printed in a size and format that was conspicuous and easily readable. If the establishment charged an automatic gratuity, it would be required to ensure that the entire automatic gratuity was distributed to the appropriate staff. If the establishment imposed a service charge where only a portion of the money would be distributed to the staff, the notice provided by the establishment would also have to include the percentage of the service charge that would be retained by the establishment. The bill would not apply to a food service establishment or caterer when serving a banquet, but would apply to that part of a food service establishment open to the general public and not serving the banquet.

An establishment that failed to provide the required notice would be responsible for a state civil infraction; the establishment could be ordered to pay a fine of not more than \$50 for a first violation and not more than \$500 for a second or subsequent violation that occurred within a 24-month period.

An "automatic gratuity" would be defined to mean money required in addition to the price of a meal, drinks or other products that was given to the staff in recognition for service provided to a customer or group of customers. A "service charge" would mean a charge that was imposed by a food service establishment and was not related to a specific service or product. A "banquet" would mean an event not open generally to the public and occurring in a food service establishment where the establishment was hired to serve food in

House Bill 4657 (3-19-02)

honor or commemoration of a particular guest, group of individuals, or occasion.

The bill would take effect 90 days after the enactment date.

BACKGROUND INFORMATION:

The bill is nearly identical to House Bill 5056 of the 1997-1998 legislative session; House Bill 5056 was passed by the House of Representatives.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the penalty provision of the bill could increase local revenue slightly to the extent that violations occurred, but the overall impact would be negligible. (3-18-02)

ARGUMENTS:

For:

Individuals working as servers in restaurants and bars are generally paid less than minimum wage by their employers, with the tips left by patrons used to “make up” the difference in their salaries between their agreed upon wages and the prevailing minimum wage. Generally, the tips received are sufficient to exceed minimum wage. This is an accepted practice among restaurant owners and their patrons and employees. The amount of the tip is usually a percentage of the cost of the meal and/or bar tab – typically ranging from 15 to 20 percent. However, many restaurants and bars have adopted the practice of automatically charging a gratuity or service charge and including that charge in the total of the bill. Most, but not all, establishments place a notice of such practice on the menu or the server may verbally inform patrons of the practice. Unfortunately, if a patron does not realize that the tip was already included in the total shown on the bill, he or she may also leave a tip on the table – in effect tipping twice. In other situations, the patron knows that the gratuity is included and may assume that the entire gratuity or service charge will be distributed to the waitstaff; however, this may not be the case. In some establishments, the employer may keep the automatic service charge or gratuity, and unless the patron left additional tip money on the table, the servers would not necessarily receive any tip money.

This can be a confusing situation for a restaurant or bar patron. No one likes to “double tip” if the automatic service charge or gratuity was indeed going to the server or servers, but some do leave extra tip money on

the table because they are concerned that the automatic gratuity or service charge added to their bills will be kept by the house and not given to the servers. The bill would eliminate this problem by requiring that all food service establishments provide a clear notice – on each bill or menu or on a poster in the dining area – as to the house policy on automatic service charges and gratuities. In addition, the bill would require that the entire automatic gratuity be given to the appropriate staff, and the notice would have to include that information. If an automatic service charge were included in the bill, the notice would have to specify the percentage of the service charge that would be retained by the establishment. The bill, therefore, would enable patrons to know - when an automatic gratuity or service charge were imposed – exactly how and to whom that money would be distributed.

Against:

The bill is not needed. The vast majority of restaurants and bars already provide notice to customers if and when an automatic gratuity charge is added. Generally, this practice is reserved for larger parties and was instituted to ensure that servers were indeed compensated appropriately. Further, even when it is clear that the tip will go to the servers, the entire tip may not go to the individuals who actually waited on the diners. Many establishments have house rules that require servers to share a percentage of their tips with the bus boys, maitre d’, and/or bartenders, yet this information is not generally shared with restaurant and bar patrons, nor would the bill require such disclosure.

Against:

Reportedly, the impetus for the bill was when a person using the services of a caterer misunderstood what the automatic service charge was earmarked for. The person assumed that the entire service charge was a tip for the servers and was upset to discover that the caterer kept most of the service charge and paid each of the servers a tip of \$40 over their wages. Under federal law, service charges are considered the property of the food service establishment. Service charges are used by establishments to cover ancillary costs such as uniforms, linens, rental costs for extra serving utensils and dishes, and so on. Service charges are most often imposed by food service establishments when catering a banquet and by hotels providing room service. Banquet servers typically are paid on a different wage scale (usually more than minimum wage) than restaurant and bar waitstaff. Generally, a caterer or restaurant will give a percentage of the service charge as a tip to the banquet servers on top of their hourly wages. However, the bill’s notification requirements would not pertain to

banquet services. Therefore, the bill would not even address the situation that was the original basis for the bill.

Even if caterers were included under the bill and so required to break down the distribution of an automatic service charge, it could only add to a patron's confusion and increase animosity between patrons and business owners because it would be difficult for a business owner to explain that general costs are written into each bill to cover breakage of dishes, damage to linens, cleaning costs for uniforms and linens, and so forth, and not the actual cost to cover those items that each catered event incurred. Some believe that requiring a restaurant or bar to disclose the percentage of an automatic service charge that was retained by the establishment (as the bill would do) could also lead to hard feelings between patrons and business owners for similar reasons.

POSITIONS:

The Michigan State AFL-CIO supports the bill. (3-14-02)

The Michigan Restaurant Association opposes the bill. (3-14-02)

The Michigan Licensed Beverage Association opposes the bill. (3-14-02)

Analyst: S. Stutzky

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.