STATE OF CALIFORNIA GRAY DAVIS, Governor

DEPARTMENT OF INDUSTRIAL RELATIONS
DIVISION OF LABOR STANDARDS ENFORCEMENT
LEGAL SECTION
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MILES LOCKER., *Chief Counsel*

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18124 Wedge Parkway, #503
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Re: Service Charge In Lieu Of Tip

Dear Mr. McInerney:

This is in response to your letter requesting an opinion from this office based on the following stated facts:

A private club in California provides dining and beverage service to its members and their guests. The club serves lunch and dinner and has a separate bar. It also provides additional services such as massages, personal training, and similar services. Generally, members simply sign a chit or invoice and are billed monthly. On some occasions members will pay by credit card and, less commonly, by cash.

The food servers, bartenders, and attendants are paid an hourly wage which significantly exceeds the minimum wage. The members are advised that an 18% service charge will be automatically added to any food, beverage or other charge. In other words, if a member comes in and orders a cup of coffee, an 18% charge will be added to his bill. The club treats this 18% as income to the club and pays sales tax as appropriate. The employees receive no part of the 18% surcharge. Employees and members are discouraged from tipping any of the employees by cash, and employees are to turn into the club any cash tips that they receive. In those instances where a member pays by the use of a credit card, the cashier adds in the 18% service charge on the credit card invoice. If a member inquires as to whether the tip is included, the employee is to state that the tip has been included.

The question you pose is whether all or any part of the 18% service charge could be considered a gratuity within the meaning of Labor Code §350(e). That issue, according to your letter, was raised because at least some members believed that the 18% service charge was being paid, in whole or in part, to the employees as a tip.

As you point out in your letter, the Division takes the position that a flat service fee imposed for banquets is income to the employer and not a gratuity. The Division had, at one time, taken the position that these "mandatory banquet service charges" were to be considered in the category of tips which had to be distributed among the workers. However, in the face of a decision by the Office of Administrative Law which the Division agreed properly analyzed the "mandatory charges", the Division subsequently has taken the position that any charge which the patron must pay, cannot be considered in the category of a "tip" which is defined in Labor Code §350(e) as a "gratuity". If funds in question were, in fact, left as a gratuity by the patron the employer would be required to pay over the entire amount to the workers. (See Labor Code §351) Such a gratuity would not, however, be wages and would not be subject to overtime calculation. (See Opinion Letter dated January 7, 1994, fn. 1)

As pointed out in the Opinion Letter dated January 7, 1994, "any charge which the patron must pay, cannot be considered in the category of a 'tip' which is defined in Labor Code §350(e) as a 'gratuity'"[1]. Evidently, the 18% service charge imposed by your client must be paid by the members and, therefore, falls into that category.

However, as the January, 1994, Opinion Letter points out, "If funds in question were, in fact, left as a gratuity by the patron the employer would be required to pay over the entire amount to the workers." Given the facts you relate, the 18% charge would not normally be considered a gratuity. However, the fact that the employer requires the employee to state that "the tip has been included" would clearly lead a patron to believe that the 18% charge includes the tip. Labor Code §356 states:

> "The Legislature expressly declares that the purpose of this article is to prevent fraud upon the public in

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[1]AB 2509, enacted by the Legislature this year, amends Labor Code §350(e) to carve out one exception to this rule, by providing that "any amounts paid directly by a patron to a dancer employed by an employer subject to Industrial Welfare Commission Order No. 5 or 10 shall be deemed a gratuity."

> connection with the practice of tipping and declares that this article is passed for a public reason and can not be contravened by a private agreement. As a part of the social public policy of this State, this article is binding upon all departments of the State."

Obviously, the required statement, at the very least, misleads the patron who is led to believe that the charge he or she is paying is, at least in part, being used to pay a tip to the employee.

There is no case law directly on point that we can point to. However, given the strong language in Labor Code §356, it is the belief of the Division that a California court, if faced with the question of whether a requirement by the employer that the employee mislead a patron into believing that a surcharge on a bill was, in fact, being paid to the employee, would conclude that such action was a fraud on the patron. Such a conclusion would lead to damages which would require that the employer disgorge the amount it had collected.

Your letter also alludes to the fact that if the patron does leave a cash tip, the employee is required "to turn into the club any cash tips that they receive." This practice violates the clear mandate of the Labor Code. All gratuities are deemed to be the sole property of the employee and may not be taken by the employer.

The Division would strongly urge you to counsel your client to change its practices in order to comply with the California law.

I hope this adequately addresses the issues you raised in your correspondence. If you have any questions, please feel free to call the local office of the Division.

Yours truly,

MILES E. LOCKER
Chief Counsel

cc: Art Lujan, State Labor Commissioner
Tom Grogran, Chief Deputy Labor Commissioner
Greg Rupp, Assistant Labor Commissioner
Roger Miller, Assistant Labor Commissioner
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