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SC Court of Appeals

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM GREENVILLE COUNTY
Common Pleas Court
D. Garrison Hill, Circuit Court Judge

Case No.: 2014-002464

Laurin Stinson,

Respondent,

v.

Hans & Franz, LLC d/b/a Hans & Franz Biergarten, Addys
Dutch Café and Restaurant, Addy Sulley, and Juergen Haubach,

Appellants.

BRIEF OF APPELLANT

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Hart v. Rick's Cabaret Intern., Inc., 967 F. Supp. 2d 901 (S.D.N.Y. 2013)

Helvering v. Davis, 301 U.S. 619, 641, 57 S.Ct. 904, 81 L.Ed. 1307 (1937)

McFeeley v. Jackson St. Entm't, LLC, No. 12 Civ. 1019 (DKC), 2012 WL 5928769, at *4 (D. Md. Nov. 26, 2012)

Reich v. ABC/York-Estes Corp., No. 91 Civ. 6265 (BM), 1997 WL 264379, at *5 (N.D. Ill. May 12, 1997)

STATUTES

29 U.S.C. § 203(m)

29 U.S.C. § 206(a)(1)

REGULATIONS

29 C.F.R. § 531.55(a)

29 C.F.R. § 531.55(b)

29 C.F.R. § 531.52

29 C.F.R. § 778.117

OTHER AUTHORITIES

U.S. Department of Labor. Wage and Hour Division. Fact Sheet # 15: Tipped Employees Under the Fair Labor Standards Act.

U.S. Department of Labor. Wage-Hour Opinion Letter 2005-31

IRS Revenue Ruling 2012-18

STATEMENT OF ISSUES ON APPEAL

Did the trial court err in its FLSA's minimum wage damage calculation performed pursuant to Respondent's motion for partial summary judgment by not recognizing the compulsory service charges paid to Respondent as a wage thereby reducing Appellants' liability and making summary judgment inappropriate in its entirety?

STATEMENT OF CASE

On May 30, 2013, Respondent filed a complaint against the Appellants alleging that they failed to pay her minimum wage and overtime during her employment as a server at the Hans & Franz Restaurant. As to the minimum wage claim, Respondent alleged that "Defendant impermissibly shifted operating costs to Plaintiff by deducting sums from her wages, thereby reducing her hourly compensation amount below minimum wage [and that] Defendant did not pay Plaintiff minimum wage during her training period." (R. p. 25, lines 15-19).

As to the overtime claim, Respondent alleged that "Defendant impermissibly calculated Plaintiff's overtime rate at 150% of her tip credit wage, rather than minimum wage. . .[thereby leading] to a deficiency in Plaintiff's compensation." (R. p. 26, lines 6-8).

After conducting discovery, Respondent seemed to abandon the overtime claim and focus on the minimum wage claim. Respondent was paid for her services pursuant to a tip credit scheme (\$2.13 per hour in direct wages + \$5.12 tip credit = \$7.25 minimum wage). (R. p. 42, lines 17-20). Essentially, Respondent's minimum wage claim rested solely on the trial court's interpretation of § 203(m) of the FLSA which lays out the rules employers must follow when they pay their employees pursuant to a tip credit scheme. (R. p. 141). 29 U.S.C. § 203(m) mandates that in order to take a tip credit the employer must: (1) inform the employee of the tip credit; and **(2) allow the employee to retain all their tips.**

Respondent made the argument that because she was not allowed to retain all her tips Appellants cannot benefit from a tip credit thereby deeming her hourly wage to only \$2.13 in

direct wages¹. (R. p. 58, lines 6-14). Respondent moved for partial summary judgment on this issue alone. (R. pp. 50-51, pp. 136-137).

Appellants argued that even if this was the case they would be entitled to an offset by the sums distributed to Respondent as service charges. (R. p. 116, lines 1-6). At the Hans & Franz Restaurant, each party of six (6) or more guests is assessed a mandatory 20% service charge added to the costs of the bill. Specifically, Appellants argued that the monies paid to Respondent as service charges were wages rather than tips; therefore, they would be entitled to an off-set against their minimum wage obligations. (R. p. 280, lines 7-16).

The trial court granted Respondent's motion for partial summary judgment in reliance of Respondent's interpretation of 29 U.S.C. § 203 and calculated her actual damages as \$9,587.25. (R. pp. 13-14). To arrive at this number, the trial court multiplied the amount of the tip credit (\$5.12) x the number of hours Respondent worked (1872.51). (R. p. 15, lines 1-4). This calculation only accounts for the \$2.13 Respondent received per hour and does not account for the service charge wages Respondent received.

Appellants timely filed a notice of appeal with the South Carolina Court of Appeals. The main contested issue pending before the Appellate Court is whether the trial court erred in its damage calculation thus making the trial court's granting of summary judgment not appropriate in its entirety.

ARGUMENT

- I. The trial court erred in its actual damage calculation for owed wages because Appellants are entitled to use the service charges they paid to Respondent to satisfy their minimum wage obligations.**

¹ Appellants had a policy in place that required all servers to return 1% of their total credit card tips in cash at the end of each shift. This policy was voted on by all the wait staff, including Respondent, who approved this policy in lieu of Appellants hiring individuals to bus the tables and share a percentage of the tips.

Employers in the United States are required to pay employees minimum wage. 29 U.S.C. § 206(a)(1). (Currently \$7.25 per hour). However, Congress has provided an exception to this minimum wage requirement in that employers are permitted to pay less than minimum wage to employees who receive tips. 29 U.S.C. § 203(m).

The mechanism that § 203(m) creates is known as the “tip credit.” The tip credit allows employers to use a portion of the employee’s tip income to supplement its minimum wage obligation to the employee, so long as the employee’s combined cash wage and tip income meets or exceeds the minimum wage.

This is exactly how the Appellants paid the Respondent. Respondent was paid a direct cash wage of \$2.13 per hour plus tips. However, as Appellants argued before the trial court, the service charges paid to Respondent are not deemed tips under FLSA and are actually wages just like the \$2.13 per hour that she was paid. Since Respondent was paid these wages in addition to the \$2.13 per hour, Appellants are entitled to use these monies to off-set their minimum wage obligations. This off-set was not factored into the trial court’s damage calculation.

- a. The services charges paid to Respondent were wages rather than tips because they were compulsory charges added to the customer’s bill and were paid to Respondent by Appellants out of the Appellants’ gross receipts.**

“A compulsory charge for service, such as 15 percent of the amount of the bill, imposed on a customer by an employer’s establishment, is not a tip and, even if distributed by the employer to its employees, cannot be counted as a tip received in applying the provisions of section 3(m) and 3(t).” 29 CFR 531.55(a) (Examples of Amounts Not Received as Tips).

Further, both the U.S. Department of Labor and the IRS treat service charges as wages and not as tips. See; 29 CFR 531.55(b); (As stated above, service charges and other similar sums

which become part of the employer's gross receipts are not tips for the purposes of the Act.).
Wage-Hour Opinion Letter 2005-31; IRS Revenue Ruling 2012-18.

Most importantly, “[w]here such sums [service charges] are distributed by the employer to its employees, however, they may be used in their entirety to satisfy the monetary requirements of the Act.” 29 CFR 531.55(b).

The service charge law was set forth to the trial court by Appellants’ citation of the United States Department of Labor Fact Sheet # 15 “Tipped Employees under the Fair Labor Standards Act (FLSA).” (R. pp. 130-132). This fact sheet further expresses what is codified in the regulations. The fact sheet defines service charges as:

A compulsory charge for service, for example, 15 percent of the bill, is not a tip. Such charges are part of the employer’s gross receipts. Sums distributed to employees from service charges cannot be counted as tips received, **but may be used to satisfy the employer’s minimum wage and overtime obligations under the FLSA.** If an employee receives tips in addition to the compulsory service charge, those tips may be considered in determining whether the employee is a tipped employee and in the application of the tip credit. (See p. 4 and Exhibit 5 of Apps’ Motion in Opp.)

By contravention, a “tip” is defined as follows:

A tip is a sum presented by a customer as a gift or gratuity in recognition of some service performed for him. It is to be distinguished from payment of a charge, if any, made for the service. Whether a tip is to be given, and its amount, are matters determined solely by the customer, who has the right to determine who shall be the recipient of the gratuity. 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. 29 C.F.R. § 531.52.

As evidenced by the aforementioned regulations, service charges tacked onto a restaurant patron's bill are clearly not tips that automatically belong to the tipped employee². There is a bright-line distinction between charges tacked on to a bill and monies that the customer gratuitously gives to the tipped employee. The most important distinction here is that service charges, when paid to the tipped employee, can be used to satisfy minimum wage obligations where ordinary tips cannot. The question then turns to whether or not the mandatory 20% fee added to six (6) or more patron's bill at Appellants' restaurant meets all the requirements of a "service charge" as such is defined by 29 CFR 531.55(a) and (b).

Appellants contend that the fees meet all such requirements because it was compulsory, and not gratuitous, and it was paid to the Respondent out of the Appellants' gross receipts.

i. The 20% fee was paid out to Respondent from Appellants' gross receipts.

Since the inception of the Hans & Franz restaurant, all parties of six (6) or more people are assessed a 20% fee for service. The computerized Point of Sale system at the Hans & Franz restaurant automatically, and without reservation of the employee, tacks a 20% fee on the total bill amount for parties of six (6) or more.

Most all courts analyzing the classification of service charge require that the monies be paid from the employer's gross receipts. McFeeley v. Jackson St. Entm't, LLC, No. 12 Civ. 1019 (DKC), 2012 WL 5928769, at *4 (D. Md. Nov. 26, 2012) ("[A]n employer must include payments in its records as gross receipts as a prerequisite to 'service charge' classification under

² Specifically speaking Respondent contends that these monies, if paid to the tipped employee, are commission payments. See 29 CFR § 778.117 (Commission Payments); Department of Labor Glossary (elaws) – Commissions (A commission is a sum of money paid to an employee based on the sale of a certain amount of goods or services. Commissions may be paid in the form of compulsory (or mandatory) service charges expressed as a specific percentage of the customer's bill).

the FLSA.” (quoting Reich v. ABC/York-Estes Corp., No. 91 Civ. 6265 (BM), 1997 WL 264379, at *5 (N.D. Ill. May 12, 1997)).

Otherwise, the charge is treated, under the FLSA, as a “tip” and may not be applied against the establishment’s minimum-wage obligations. In a recent District Court opinion, the Court explained the logic behind why such monies have to be paid from the establishment’s gross receipts in order to qualify as a service charge. Hart v. Rick’s Cabaret Intern., Inc., 967 F. Supp. 2d 901 (S.D.N.Y. 2013). Hart involved exotic dancers who alleged they were misclassified as salary exempt and sought owed minimum wages pursuant to the FLSA. One of the issues in Hart was whether the performance fees set by the night club and paid to the dancers for time spent with the customers was a service charge or a tip. Hart, 967 F.Supp. 2d at 927. If the money was deemed a service charge then the night club could off-set any owed minimum wage claim by amounts paid out as service charges.

In addressing the gross receipt requirement, the Court in Hart explained;

The requirement of inclusion in gross receipts advances the FLSA’s goal of assuring that the employee is paid, with mandatory deductions taken from the employee’s wages. These deductions (e.g., Social Security, Medicare) are taken in the employee’s longer-term interest, to assure, e.g., her retirement security. See Helvering v. Davis, 301 U.S. 619, 641, 57 S.Ct. 904, 81 L.Ed. 1307 (1937) (purpose of FICA taxes is “to save men and women from the rigors of the poor house as well as from the haunting fear that such a lot awaits them when journey’s end is near”); Bowman v. Stumbo, 735 F.2d 192, 196 (6th Cir.1984) (these tax programs were “created by the Social Security Act of 1935 as a part of the comprehensive program for implementing old age benefits on a national level”); Greenwald v. United States, No. 98 Civ. 3439(DC), 2000 WL 16939, at *2 (S.D.N.Y. Jan. 10, 2000) (“The purpose of FICA taxes is to fund a national system of social security and [M]edicare health programs.”). Requiring that service charges pass through the employer’s gross receipts guarantees that the employer takes responsibility for its employees’ wages, and effectively guarantees that such mandatory deductions are taken. By contrast, where customers pay employees directly, and the employer is left out of the payment process, there is no assurance that such deductions will be taken.

Hart, 967 F.Supp. 2d at 927.

The service charges at issue in the present matter were paid from the Appellants' gross receipts. These fees can be seen on the Point of Sale documents generated by Respondent and submitted to the trial court. (R. pp. 122-129). These documents contain Respondent's gross receipts, charged tips, and service charges for every two weeks of her employment. The service charges are under the heading "Svc Charges." The corresponding numbers are composed of the 20% fees that were added to the bill for six (6) or more guests. The Respondent was paid these monies along with her charged tips and her hourly wage of \$2.13 in a bi-weekly paycheck. The mandatory deductions, FICA, Medicare, Social Security, and state taxes, were deducted from the charged tips, the hourly wage, and the service charges paid to Respondent.

Ultimately, these monies were service charges as such are defined by the Department of Labor regulations. The regulations are clear that if these monies, which belong to the employer, are paid to the employee they can be used in their entirety to satisfy minimum wage obligations. 29 CFR 531.55(b).

The Trial Court erred in only considering the \$2.13 hourly wage Respondent made while employed with the Appellants. The service charges, like the hourly wage, should have been accounted for during the trial court's damage calculation.

CONCLUSION

The 20% fee added to each party of six (6) or more guests at Appellants' restaurant is service charge under the law. Service charges can be used to satisfy minimum wage obligations. The Court erred by not considering these wages in their minimum wage damage calculation. Appellant seeks from this Court a remand to the trial court to conduct a new damage calculation

considering the arguments above and reversal of summary judgment in Respondent's favor for all weeks in which she made an excess of \$7.25 per hour.

Respectfully Submitted,

A handwritten signature in dark ink, reading "John G. Reckenbeil". The signature is fluid and cursive, with the first name "John" being the most prominent. The signature is written over a horizontal line.

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CERTIFICATE OF COUNSEL

I, John G. Reckenbeil, certify that this final Brief of Appellant complies with Rule 211(b)
as set forth in the South Carolina Rules of Appellate Procedure.

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Dated: March 23, 2015
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