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Federal Court Dismisses Lawsuit Against New York City Restaurant That Imposed Auto-Gratuities . . . But Don't Start Putting Them Back Just Yet

By Glenn S. Grindlinger

Some New York City restaurants assess an automatic gratuity that customers pay, usually without questioning the charge. From an employment law perspective, there are many problems with these automatic gratuities, not the least of which is that their use impacts the employer's ability to take a tip credit towards its minimum wage obligations for those employees who are the beneficiaries of the automatic gratuity. From a consumer law perspective, automatic gratuities are even more problematic because New York City law specifically prohibits restaurants from assessing a surcharge to listed prices. Nevertheless, recently, a federal court in Manhattan dismissed a class action where the plaintiff alleged that the restaurant assessed an automatic gratuity in violation of applicable law. While the decision is welcome news to the restaurant industry, it does not impact New York City's prohibition against assessing surcharges to listed prices, which in many cases prevents restaurants from imposing automatic gratuities. Accordingly, restaurants and other hospitality enterprises should be careful not to read too deeply into this decision.

In 2013, Ted Diamond filed a class action complaint against Darden Restaurants. The complaint alleged that Darden engaged in unfair business practices and otherwise violated the law by: (1) assessing an automatic, nondiscretionary gratuity of 18 percent on customer tabs; and (2) failing to include the prices of all beverages that it offered in its menus. On July 9, 2014, a Manhattan federal court dismissed the lawsuit on technical grounds. A brief description of the court's decision and its reasoning is set forth below.

With respect to the automatic gratuity, Mr. Diamond alleged that the charge violated New York City Administrative Code §20-700, which prohibits businesses from engaging in unfair trade practices, and New York City Rule §5-59, which prohibits restaurants from "adding a surcharge to listed prices." Mr. Diamond claimed that the automatic gratuity was such a surcharge and therefore was impermissible under New York City law. He also alleged that by violating §20-700 and §5-59, Darden violated New York General Business Law (GBL) §349, which prohibits businesses from engaging in deceptive acts or practices.

The court easily dismissed the automatic gratuity claim for four reasons. First, it noted that there was no private right of action for violations of §20-700 or §5-59 (that is, an individual could not bring a lawsuit for their violation although the government can still do so), a fact conceded by Mr. Diamond. Second, Mr. Diamond could not circumvent the lack of a private right of action by asserting a claim under GBL §349. Third, Mr. Diamond did not allege that Darden had engaged in a "materially misleading act or practice," a prerequisite for prevailing

on a GBL §349 claim, as it was clear from the face of the complaint that Darden had specifically informed Mr. Diamond (and presumably other customers) about the automatic gratuity. Fourth, the court found that Mr. Diamond had not alleged an injury that was separate and distinct from the purported deceptive act. In order to assert a claim under GBL §349, the deceptive act must cause the injury but it cannot be the injury. Therefore, in most cases under GBL §349, the deceptive act is the false or misleading label and the injury is the purchase price. Mr. Diamond claimed that the false act was requiring patrons to pay the automatic gratuity and the injury was the amount of the gratuity. Thus, Mr. Diamond had alleged that the deceptive act and injury were one and the same and this was insufficient under GBL §349.

As for Mr. Diamond's claim that Darden violated the law because the menus did not list the price of every beverage that was available, the court dismissed this claim holding that Mr. Diamond lacked standing to assert it. In order to assert claim in court, the plaintiff must allege that he or she suffered a cognizable injury; if the plaintiff fails to do so, the plaintiff does not have standing and the court has no jurisdiction over the dispute. The court found that Mr. Diamond had not alleged that he was injured by Darden's failure to list all the prices for all of the beverages that it served. Specifically, Mr. Diamond claimed that he purchased a Coke at Red Lobster (a restaurant owned by Darden) and was charged $3.09, but the price was not listed the menu. However, he did not allege that he did not receive the beverage; he did not allege that he would not have purchased the beverage had the price been listed on the menu; and he did not allege that beverage prices at Red Lobster were significantly more costly than at other restaurants. Rather, his "injury" was predicated on the fact that the prices of certain beverages were not listed. This is not a cognizable injury and therefore the court dismissed this claim for lack of standing.

While this decision is helpful to the restaurant industry, it is not a panacea. It is helpful that the court confirmed that §20-700 and §5-59 do not have private rights of action and therefore aggrieved individuals cannot file a claim in court for their alleged violation. However, for the most part, the decision merely dismissed the class action lawsuit on technical issues that might have been avoided had the complaint been drafted better. Further, the decision will not have any impact on whether state or local agencies, such as the New York Department of Consumer Affairs, can file actions against employers who violate §20-700 or §5-59. Instead, the decision should be a reminder to restaurants that, generally, they cannot assess automatic gratuities on customer tabs and they must list the prices of all beverages in their menus.

For more information about this Alert, please contact Glenn S. Grindlinger at 212.905.2305 or ggrindlinger@foxrothschild.com or any other member of Fox Rothschild's New York Labor and Employment Department.

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