case study

Where's My Slice of the Apple? A Case Study

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Description and Background of Company

This case study sets out to allow the reader to review and understand one restaurants management employee issue that arose out of new technology. The study will review law, management, employee education and risk management after the description of the restaurant and other impacting factors.

Applebee's is a full service restaurant, serving American food with casual dining table-service that serves lunch, dinner and late night fare. The menu consists of basic American dishes such as chicken, steak, shrimp, salads, pastas and desserts. Their alcoholic drink menu is also Americanized and includes such beverages as mixed drinks, martini's, beer and wine.

Applebee's was established in1980 under the name of TJ Applebee's Rx for Edibles & Elixirs from the original owners, Bill and TJ Palmer. From its origins, the restaurant was very popular and grew quickly. Within just a few years, it started to set up franchises.

Currently, Applebee's is owned by Dine Equity which also owns IHOP (International House of Pancakes), another franchised restaurant. Applebee's is the #1 casual-dining restaurant chain, with about 2,000 locations in the US and about 20 other countries, offering a wide variety of appetizers and entrees . The majority of the restaurants have been franchised. Recently, the company sold over 475 company-owned stores in the US to Franchisees, which translates to the company being 99% franchised . That number continues to rise as the company transitions to an all franchised model.

In the publication, Restaurant News, an article rated the casual-dining brands whose customers were most likely to visit it most often due to its "good selection of alcoholic beverages". The article rated Buffalo Wild Wings as 1st, with 29% of its customers citing the alcoholic selection as their reason (multiple responses allowed). Applebee's came in 2nd place with 24% of its customers citing that reason. Outback Steakhouse and T.G.I. Friday's tied for 3rd place with 22%" . Applebee's is also listed as the #1 Casual Dining chain in Full Service Restaurant (FSR) Magazine. In FSR magazine, the other top ranking casual dining restaurants are #2 Chili's, #3 Olive Garden, #4 Red Lobster and #5 Buffalo Wild Wings (FSR 50, 2013). In addition, Applebee's is ranked as the #2 most innovative company according to Fast Company.com. (Staff, 2013). In an interview in July of 2012 going over the revitalization of Applebee's, Mike Archer, President of Dine Equity's Applebee's division, explained that steak is the most popular menu item as they "sell more steak than anyone in the bar and grill category."

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The company, applauded for its awareness of popular menu items, tends to cycle through or update similar options. In the news in Nov 2013, it was outlined that the company brought back the menu items that are cooked with alcoholic beverages such as beer, wine and tequila because they had been popular favorites .

These details show continued improvement and that the company is doing well and still finding ways to expand their services. One would foresee additional expansion and growth for the company as its popularity continues to rise both in the United States and internationally. "Applebee's International Inc. has more than $4.5 billion in U.S. system wide sales. It's a division of Glendale, Calif.-based Dine Equity Inc., the publicly traded company (Ticker: DIN) that also owns IHOP Corp. Applebee's was acquired by IHOP in 2007, and the combined company became Dine Equity" . The acquisition of Applebee's by IHOP (Dine Equity) was followed by even more changes and updates. IHOP was an almost all franchised brand (99%) at the time of the acquisition and the new company plans to do the same for Applebee's. At the time, once the merger was finalized, the new, Dine Equity was the owner of the largest number of full service restaurants in the world. Chairman and Chief Executive Officer Julia Stewart stated in a press release for the acquisition that "Applebee's meets all of our acquisition criteria and we expect the combination to generate significant additional value for our shareholders." The basic outline provided a detailed plan to increase cash flow, lower overhead cost and create value. The press release was as follows:

- Franchising the majority of Applebee's 508 company-owned and operated restaurants;
- Reducing related General & Administrative expenses as those restaurants are franchised;
- Selling Applebee's-owned real estate and executing related leasebacks;
- Reducing capital expenditures as Applebee's is transitioned quickly out of its more capital intensive company operations model; and
- Re-energizing Applebee's brand, driving same-store sales performance and improving the system's operational performance and profitability.

Since the merger, Dine Equity has continued to update their business model and expand their product offering. One of the more recent updates to the chain is extended hours and curbside pick-up. Dine Equity continues to be in the headlines as it makes these dramat-

Figure 1

Old and New Restaurant Models

Old (as of 2010)

New (as of 2013)

ic moves and updates its structure. The old and new restaurant models are shown in Figure 1.

As of Tuesday, October 29, 2013, it was reported that "Companies such as Dine Equity and Burger King Worldwide Inc , which on Monday reported a better-than-expected quarterly profit, are moving to a mostly franchise model that provides a steady and lower-risk stream of revenue. A 43 percent decline in expenses helped Dine Equity to post a third-quarter profit that topped Wall Street estimates, even as revenue fell 25 percent."

Essentially, with the merger, the sale of company owned stores and upgrades to the brand, show that the company has cut their additional costs and now have the opportunity to focus on profit generation. The additional increase in profitability for the company will be in full effect once the transition to franchised restaurants is completed. It is expected that the next few years will show a steady increase of profits and the main revenue source will be from the franchisees, again, allowing Dine Equity to focus on new ventures for the restaurants.

Found on the Applebee's website and on Dine Equity's corporate website, the timeline below outlines how Applebee's has continued to grow and enhance services and options (Table 1& Figure 2).

What is a Franchise?

A franchise is a legal agreement granting rights to sell products and services in a specified manner. There is usually a formal document called the Franchise Disclosure Document (FDD) that outlines the specific details of the agreement. These legal agreements outline items such as use of product, trademark, location of services, i.e. territory, marketing plan, training, financing and so on. The Franchisor grants the rights of use to the Franchisee as a method to distribute the goods or services owned by the franchisor. This relationship of the Franchisor and Franchisee normally has a set of a few items that each side of the agreement will bring to the table/agreement. . Basics of franchise agreements are listed in Table 2.

Essentially, the franchisee, with the support of the franchisor, will maintain a section of the franchisors' business, usually at a specified location or area where the operations of the franchisee will bring in revenue for both the franchisee (direct) and franchisor (franchise and royalty fees). Franchisors tend to choose to franchise in order to

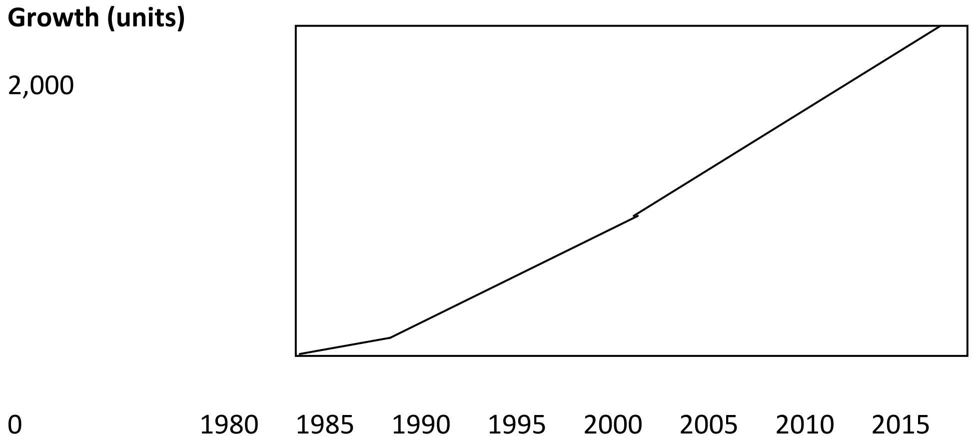
Table 1

Applebee's History

- 1980 Bill and T. J. Palmer opened T.J. Applebee's Rx
- 1983 Bought by WR Grace & Co.
- 1985 First Franchised
- 1989 Went public as Applebee's International
- 1998 Grew to over 1,000 Restaurants
- 2004 Partnership with Weight Watchers Menu & Carside To Go pickup service
- 2005 Goes International – Brazil, Chile, Ecuador & Jordan
- In 2007, Applebee's stopped offering new Franchises in the USA, only internationally
- 2010 Revitalized concept updating the look and atmosphere
- 2012 There were 2,034 Applebee's in 49 States and 15 International countries & 28,000+ Employees

Figure 2

Applebee's Growth



expand the base offering of their products or services, so they might generate more revenue and reduce expenses. Some examples of well-known franchised restaurant chains are McDonalds, Wendy's, Subway, IHOP, Chili's and Applebee's.

Issue, Impact and Dilemma

Although Applebee's is quite large, and extraordinarily popular, it too has the same issues as small town restaurants. Specifically, there are staff issues with management and vice versa. These small issues can become national news swiftly as Applebee's is an international franchise, so there is significant interest in the happenings of the chain from the public, shareholders, and other franchise owners. One such article dated October 2007, describing a server's compensation lawsuit (explained in detail below), stated that this lawsuit 'could change labor practices in the full-service segment.' This and many additional articles around the same time period outlined that over 40,000 current and former restaurant employees could potentially be represented in this case, resulting in heightened interest throughout the industry by any tip based employees and companies who employ them.

In a legal case (Gerald Fast vs. Applebee's), there is an examination of the working hours of the tipped wait staff and the minimum of 20% of time worked applied towards other than waiting tables/tip-able duties and how this became such a hot topic. The initial lawsuit over wages for servers filed in 2006, and which has expanded over time to include time spent on non-tipping duties by servers of the company, has frequently been in the news ever since.

Gerald Fast worked at Applebee's at the Jefferson City, Missouri location for a few years and ended up as a bartender in 2005. He earned tips while he served customers. He earned no tips while cleaning and restocking the bar.

From the court document, filed May 3, 2007, the Columbia restaurant was owned by Ozark Apple's Inc. (Ozark), which was an Applebee's franchise through May 2005 when ownership of the restaurant went to Gourmet Systems, Inc., an Applebee's subsidiary . Mr. Fast worked as bartender earning the tip minimum of 4.75 per hour plus tips. Mr. Fast also "stocked the bar, cleaned up the adjacent restaurant area, arranged seating, mopped the floor, cleaned bar appliances and dispensers, took inventory, and answered the phone." (As per the letter). These extra items that Mr. Fast was required to do by management

Table 2

Franchise Agreement Basics (Source: Khan, 1999)

Franchisor agrees to provide:	**Franchisee agrees to:**
• the rights of use (trademark, copyright, etc.) • training • marketing (corporate) • research • product	• providing financing (capital to start up and run) • basic knowledge with continual learning of product • maintain standards set forth by franchisor

were not tip earning duties. However, his total income was well above minimum wage when adding in the tips he received.

During this time, Applebee's had the minimum wage match policy, called 'tip credit' that guaranteed that the employee working off tips ended up with at least the minimum wage for each hour that was worked. In addition, Applebee's also had a requirement that the employees were to report to work 15 minutes prior to when their shift was supposed to begin.

Applebee's maintained employee's schedules by using automated time keeping systems where employee's clocked in and out at the beginning and end of their shifts. With the early arrival policy in place, employees could clock in immediately, but their time was not counted until their shift started. So, even though Mr. Fast would clock in the time of arrival, which was 15 minutes prior to his shift, he was often asked to start working immediately and 1 to 15 minutes of that time would not be counted towards pay.

In 2006, Mr. Fast filed lawsuits against Applebee's in regards to tips, pay and time management for employees who are tipped employees and are paid hourly at a lower rate than minimum wage as they fall under the US Labor law, Fair Labor Standards Act (FLSA). Tipped employees are defined by the US Department of Labor as employees who earn over $30 per month in tips. The wages under FLSA for tipped employees are the property of the employee.

Specifically, Mr. Fast believes that the two claims that were outlined in the court document filed May 3, 2007, violate his 2nd amendment rights by violating the FLSA as follows:

- Applebee's did not pay him minimum wage while he was performing his non-tipped duties.
- Applebee's did not pay him for the entire time the he worked as he had to arrive early, but was not paid until his actual shift started .

Currently, under the Fair Labor Standards Act (FLSA), employers must pay their employees a minimum wage of 7.25 per hour ($5.15 in 2005) unless they are a tipped employee. For tipped employees, employers have the option to pay a lower cash wage minimum (different per state) and take a 'tip credit.' A tip credit is a credit used to balance the pay of the employee to reach the minimum wage .

A tip credit is shown as a credit against the minimum wage requirement for pay to an employee. As an example, the minimum wage is $7.25, the minimum cash wage is $2.13. For a tip credit, the employer would be able to balance the difference to ensure the employee would receive at least minimum wage (7.25 - 2.13 = $5.12) Thus, $5.12 is what the employer can claim as a credit toward their taxes. If the tips do not cover the difference to bring the employee to the minimum hourly wage, then the employer is to pay the difference to the employee.

According to the FLSA regulations there are three categories for tipped employees:

1. All tip producing duties – employer can take tip credit
2. If the employee is not tipped but he must assist another employee's tip producing duties – employer may take tip credit that employee spent on non-tipped duties as long as not over 20%
3. Non-tipping duties – employer cannot take tip credit

Mr. Fast provided evidence he felt showed that not only was Applebee's depriving him of time worked, but also that the tip credit was not applied correctly to hours that he had worked while not being able to earn tips.

Applebee's response to the lawsuit was that the job description of being a bartender included these non-tipping activities, with the understanding that these activities would not take more than 20% of his time. In addition, Applebee's points out that their employee handbook alerts employees to limit the non-tipping duties to less than 20%, so that the employee is responsible for keeping his time.

The allegations against Applebee's by Mr. Fast quickly became news headlines due to the fact the Applebee's was a national chain. The case was watched closely by companies with tip-based employees, by tip based employees themselves of course and by the department of labor with its direct involvement.

Applebee's alerted the courts that Mr. Fast worked time was so minimal that it should not be necessary to review how much time was truly worked and for compensation. The court stated that he could file a claim for unfair labor practices outlined above to seek recovery for claim on early clock in. T courts sided with Mr. Fast in that there was enough time missing for pay which was questionable. Although, there was no formal evidence, there was enough information on his allegations to show that this case should be taken to trial.

By June of 2007, the Federal Judge granted the lawsuit class-action status. This means that current and former employees could now join the lawsuit against Applebee's as it pertains to more than just Mr. Fast. In addition to allowing the class action, the judge also ordered the company to provide a list of current and former employees that would be eligible to join the lawsuit .

In the court document filed in August of 2007, Applebee's submitted an appeal and amendment to the definition of 'tipped' employees suggesting that the definition was not correctly interpreted and that Applebee's was actually following the 20% rule set forth by the Department of Labor in 1988 . Applebee's even went to the Department of Labor requesting an update to the interpretation. However, the court did not agree with Applebee's at the time and the courts did not approve Applebee's claim of an incorrect definition to be an item that would cease the proceedings or change the course of the lawsuit. The courts did, however, acknowledge that there could be a resolution in the future on the definition of tipped employees .

A letter went out on September 7, 2007 to approximately 60,000

Table 3

Timeline of the Law Suit

- Filed in July 2006
- August 2006 Class action lawsuit accepted by the courts
- September 2006 Letter sent to current and formal employees to join lawsuit
- August 2007 Applebee's appeal and questioned definition of non-tipped employees
- March 2010 Courts agreed that the Plaintiffs evidence was strong, then requested records detail be provided
- May 2011 Ruling confirming required pay minimum wage on non-tipped duties over 20% of time
- Settled September 2012 where Applebee's paid plaintiffs' a total of $9 million. Case dismissed.

former employees of Applebee's, who were employed anytime from June 19, 2004 to the time of the letter, to inform these former employees of the lawsuit and to advise them on their rights that may have been affected in the lawsuit and that they were eligible to participate in the lawsuit. (Letter is appendix a) The letter goes on to explain an outline of the lawsuit and that they may join if they feel they were not properly compensated as servers or bartenders working at an Applebee's. Subsequently, after receiving the acceptance letters from former employees, the total that the lawsuit included was over 5,000 servers and bartenders.

As a part of the proceedings the courts looked deeper into the Fair Labor Standards Act and recited much of the detail in the law in order to find a better understanding of fairness in this case which was outlined in the court documents for the case filed March 4, 2010. A focused outline stated, "An employer is specifically directed by the department of labor to keep separate records for tipped and non-tipped occupations." The outline then goes on to review the fact that some tipped employees are to partake in non-tipped duties, however, this does not mean that these tipped employees time would not be considered for the tip credit. The case then cites the Department of Labor's Field Operations Handbook to review the detail explaining that the only consideration outside of the tip credit for a tipped employee would be if there was more than 20% of time spent on non-tipped work. The times when the employee goes over the 20% do not fall under the tipped employee regulation .

According to Mr. Fast and waiters et all, the plaintiffs, many times the staff was required to work non tipped work such as cleaning and set up prior to opening of the restaurants, cleaning during their shifts and cleaning after as well as other duties such as rolling silverware. The plaintiffs also specified these duties were not specific to customers they would be serving under the tip based work and as these activities covered over 20% of time spent on these activities, Applebee's should not have taken tip credit, yet they did so they are asking specifically for the additional pay. Again, Applebee's stated that they had not violated the FLSA in that the 20% rule from the Department of Labor's Handbook does not match the terms in the FLSA which focuses more specifically on the occupation of the employee, not the employee's duties which would then allow the payment to the tip based employees to fall completely under the tip credit rule. Again, the courts sided with the plaintiffs in that more detail needed to be reviewed in order to find a formal judgment in the case. However the Department of Labor Regulation 531.56(e) and the Department of Labor's Handbook section 30d00(e) legally outlines the definitions of tipped employee pay. These arguments have provided the court's decision to request that Applebee's provide formal records of the time spent on certain duties. Further outlining that the courts understanding of how Applebee's was reading the law was that they could require their servers and bartenders to perform non-tipped duties to an unlimited extent, which is not what the law was meant to outline. The definitions and laws were reviewed in detail, and other court cases with similar arguments were also reviewed in order to find a better understanding of what outcomes there should be here.

As a side note, FLSA did not outline tips or tip based employees which, prior to the additional definition, allowed employers to take tips. By 1974 tipped employee definition and rights were outlined as to be able to keep tips. However, in 1988, the DOL Handbook finally included detail on the 20% maximum for tipped employees to be working non tipped work.

In early 2011, the case was reviewed and sent back to lower court to rule on the case. A ruling in May 2011, against Applebee's, confirmed that if a tipped server spends more than 20% of their time on non-tipping activities such as cleaning restrooms, they are entitled to minimum wage. As these rulings affect the nation and not just in the restaurant business, many employers and employees are now ensuring they keep accurate and up to date documentation of duties performed, tipped and non-tipping work done.

The issues were still not resolved completely between Applebee's and Fast, former employees ET all. There was finally a settlement made where Applebee's agreed to pay $9 million to Fast and the wait staff who participated in the lawsuit. Shortly after the settlement, the case was dismissed without a formal ruling specific to both claims by Fast and by the former employees. The timeline of the law suit is shown in Table 3.

Conclusion

This case study highlights the issue of a tipped employee's time versus his wages from both the employee and employer perspective. It outlines how small adjustments to time and pay can pose a huge issue for both the employee and the employer, specifically in the case of Fast vs. Applebee's.

The interpretation and understanding of laws from each perspective provides a fuller understanding of what each party has determined to be correct and accurate. Applebee's and employees of Applebee's will have a much better definition of time worked and documented hours of shift pay and detail on duties to be performed.

The circumstances of the Applebee's case are not unique to this one restaurant chain, so that the outcome of the more defined review of definitions made by the FLSA will assist both employers and employees of all restaurants in the future. This means that it is likely many more tipped employees will reference this case in their own proceedings and submission for request of fair labor practices.

Questions for Discussion

- Does 20% of a tipped employee's time used for non-tipped duties need to be adjusted?
- If you could come up with a way to pay tipped employees, how would you formulate this?
- How many hours does a specific individual work on non-tipped work a week?
- From the employer's perspective, what sort of written policy would you have regarding the tipped employee?
- Outline of tipped compensation for employees
- Directed to work 19% or less to avoid having to pay tipped employees minimum wage
- From an employer's perspective, what policy would you put in place to track the tipped employee?
- From the employee's perspective, what written policies have you read that provide guidance? Were you aware of such policies being available for you?
- From the employee's perspective, if you had written guidance to divide time in various tasks, would you be able to manage keeping track of this?
- As an employer, what time accounting system would you have in place?
- Internal compliance?
- Management training?
- A software package?
- What would be a circumstance in which the employer may need to request that the employee work over the maximum of 20% of their time on non-tipping duties?
- If you determine the employee is working 20% or more on non-tipped duties, what actions would have to be taken?
- Was the issue with the time-clock machine or with the policies of Applebee's?

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