



Discussion paper

A within-restaurant analysis of changes in customer satisfaction following the introduction of service inclusive pricing or automatic service charges[☆]



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ABSTRACT

Many U.S. restaurants have recently adopted no-tipping policies or are considering doing so. This study examines the effects of such moves away from tipping on restaurant's online customer ratings. The results indicate that (i) restaurants receive lower online customer ratings when they eliminate tipping, (ii) online customer ratings decline more when tipping is replaced with service-charges than when it is replaced with service-inclusive-pricing, and (iii) less expensive restaurants experience greater declines in online customer ratings when replacing tipping with either alternative than do more expensive restaurants. These findings provide a strong argument for the retention of tipping, especially among lower- and mid-tier restaurants.

1. Introduction

Tipping is widespread in U.S. restaurants, but a growing chorus of journalists, policy analysts, and social commentators have called for its replacement with service-charges or service-inclusive-pricing (see Ghenis, 2015; Grimminck, 2015; Keane, 2014; O'Neil, 2015; Palmer, 2013).¹ Moreover, many restaurateurs have heeded these calls. A recent American Express survey of 503 U.S. restaurateurs found that 18 percent had already adopted no-tipping policies, 29 percent were planning to do so, and 27 percent might consider doing so in the future (Crowley and Rami, 2016). These actual and contemplated moves away from tipping are motivated in large part by the recent increases in the legal-minimum wage and the commensurate rise in back-of-the-house labor costs. Many restaurateurs hope to offset such costs by replacing tipping, which generates revenue management cannot legally access, with service charges or higher menu prices, which generate revenue management can control and distribute more equitably between front- and back-of-house employees (Lynn, 2017a).

However, the benefits and costs that restaurateurs must consider before replacing voluntary tipping with alternative compensation structures goes well beyond simple labor cost calculations. While a thorough review of the pros and cons of tipping versus its alternatives is well beyond the scope of this paper (see Lynn, 2017a for such a review)

one particularly important factor that restaurateurs should consider if deliberating about abolishing voluntary tipping in their establishments is the effect that such a decision may have on overall customer satisfaction. While there are theoretical reasons to expect that voluntary tipping may either enhance or undermine customer satisfaction vis-à-vis service charges and service inclusive menu pricing there are unfortunately a shortage of published studies that restaurateurs can consult, which have directly assessed customer satisfaction under these various compensation structures.

In fact, we are aware of only one study that has centered on the relationship between customers' overall dining satisfaction and restaurant tipping policies (). In this study the author reported overall dining satisfaction to be reduced in Joe's Crab Shack establishments after replacing voluntary tipping with service inclusive pricing. Whether these results can be generalized to other restaurant concepts is unknown. Moreover, there have been no studies done in the restaurant context that have assessed changes in overall dining satisfaction after replacing voluntary tipping with automatic service charges. As such, even if Lynn's (Forthcoming) results can be replicated it remains unknown whether consumer satisfaction would be enhanced, remain the same, or reduced if restaurants replaced voluntary tipping with automatic service charges rather than service inclusive pricing. Further, to our knowledge there are no published studies that have explored

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¹ In the United States, restaurants eliminating tipping forgo a tip credit that allows them to pay tipped workers a lower minimum wage. Thus, restaurants without tipping have higher labor costs that must be offset by either service charges or higher, service-inclusive menu prices. Restaurant profit margins are not high enough to eliminate tipping and pay higher wages without generating additional revenue via service charges or price increases. As such, alternative compensation structures aside from those considered here (voluntary tipping, service inclusive pricing, and automatic service charges) are extremely rare.

restaurant-level characteristics associated with potential increases/decreases in customer satisfaction following the implementation of no-tipping compensation policies (e.g., automatic service charges or service inclusive pricing).

In response, this paper begins with a brief review of the theoretical processes that may produce either positive or negative tipping policy effects on customer satisfaction. Based on this review we posit that customer satisfaction will on average be greater under voluntary tipping than under a service inclusive pricing or automatic service charge structures. Next, we outline theoretical reasons that lead us to expect that such tipping policy effects on consumer satisfaction will be stronger in less expensive relative to more expensive restaurants. Finally, we test these predictions by analyzing online satisfaction ratings of customers' dining experiences within restaurants that operated under different tipping policies between September 1, 2014 and August 30, 2016. In doing so this study offers a direct test of the within-restaurant changes in customer satisfaction that stem from the introduction of no-tipping compensation policies and identifies restaurant price as an important determinant of successful implementation of such policies.

2. Literature review and hypotheses

There are some theoretical reasons to believe that customer satisfaction will be higher under service charges or service-inclusive menu pricing than under tipping. In particular, it is possible that replacing variable tip income with more certain wages will improve the customer experience by (i) attracting more professional wait-staff (Parise, 1987), (ii) allowing servers to focus on providing good service instead of worrying about tips (Porter, 2013; Fulton, 2016), (iii) encouraging more service-enhancing teamwork (Frumppkin, 1988), and (iv) reducing incentives to discriminate against consumers who are predicted to tip them poorly (Barkan and Israeli, 2004; Brewster, 2015).

While each of these four processes are likely to sometimes undermine customers' dining experiences, the available published empirical evidence leads us to be skeptical that the cumulative effects of such processes are sufficiently strong to compromise consumers' overall dining satisfaction. For instance, extant studies have shown that those who prefer working for tips are more likely to be experienced wait-staff, possess more service oriented attitudes, and be more satisfied with their job than those who prefer working under an automatic service charge compensation system (see Lynn, 2017b; Lynn et al., 2011). While the strength of these associations tend to be quite weak they nevertheless suggest that tipping may selectively attract, rather than discourage, more committed and professionally oriented waiters and waitresses.

Second, the contention that the uncertainty inherent in voluntary tips encourages servers to obsess about being compensated for their efforts and as such are distracted from providing optimal service to their customers (Porter, 2013; Fulton, 2016) assumes that the average server does not see a clear connection between the tips they receive and the quality of the service they provide. However, extant studies indicate that this is not the case. Rather, the vast majority of servers have been shown to perceive a moderate to strong relationship between service quality and the size of the tips that they receive (Kwortnik et al., 2009; Lynn et al., 2011). Thus, rather than functioning to distract servers from providing high quality customer service these findings suggest the opposite—most servers are motivated to provide high-quality service, in part, because they trust that their efforts will in fact be rewarded with a fair tip.

Third, the argument that tipping may function to discourage servers from working together as a team and, thereby, lower overall customer satisfaction (see Frumpkin, 1988) is logical, but likewise suffers from a lack of substantiating empirical evidence. In fact, to our knowledge there have been no studies that have directly compared cooperative server behaviors across tipped and non-tipped restaurants. Nor are there any published studies that have assessed within-restaurant

changes in cooperative server behaviors after implementing non-tipping compensation policies. Moreover, the limited indirect evidence of this process that is available (see Barkan et al., 2004) suggests that any increase in cooperative service behaviors that might result from abolishing voluntary tipping is not likely to outweigh the resulting decrease in individual server motivations that stems from the widespread belief in the service-tip contingency (see Lynn, 2017a).

Finally, it has been argued that voluntary tipping undermines consumer satisfaction by encouraging servers to discriminate against patrons who are predicted to tip them poorly. Unlike the previously discussed theoretical processes by which voluntary tipping may undermine customer satisfaction there is a growing body of empirical evidence indicating that servers may in fact withhold effort from customers perceived to be poor tippers (e.g., Barkan and Israeli, 2004; Brewster, 2015b; Lynn, 2017a,b). For instance, Barkan and Israeli's (2004) research found that servers are quite proficient at predicting the size of tips that their customers will actually leave, in part, because they manage the service encounter to ensure that their predictions materialize. That is, when servers predicted a poor (good) tip they subsequently tended to exert less (more) effort during the service transaction thereby decreasing (increasing) the size of the tip that was actually left. Customers who are members of social aggregates that are perceived by servers to be on average poor tippers, including racial/ethnic minorities, women, teenagers, elderly adults, tables with small children, and Christians have been shown to be particularly vulnerable to this tip-driven discriminatory service (see Brewster, 2015).

It nevertheless remains questionable whether tipping motivated service discrimination becomes manifest in consumers' overall satisfaction with their dining experiences. For instance, research documenting the strength and pervasiveness of servers' cynicism towards the tipping practices of Black Americans, in particular, led Brewster and Brauer (2017) to posit that these customers would on average report diminished dining experiences relative to their White counterparts. However, in contrast to the authors' prediction, Black and White consumers in a non-representative but geographically diverse sample were found to report similar levels of satisfaction across nine distinct measures assessing their typical and recent dining experiences. Further, where interracial differences were observed, Black respondents were found to report slightly more positive and less negative experiences than Whites. These results were largely consistent with those observed in an exit survey of customers leaving a moderately priced restaurant in Detroit, Michigan (see Brewster et al., 2014). While more research assessing the nature of tip-driven service discrimination and the conditions under such discrimination is likely to become manifest in customer reported dining satisfaction is clearly needed the evidence that is available fails to support the contention that replacing voluntary tipping with either service inclusive pricing or automatic service charges would result in a notable increase in average level of satisfaction among members of social groups that are thought to be inadequate in their tipping practices.

In contrast to the aforementioned lines of argumentation underpinning proponents' of non-tipping compensation structures there are more empirically supported theoretical reasons to infer that customer satisfaction may be higher under tipping than under service charges or service-inclusive menu pricing. First, the performance contingent nature of tipping helps to attract more service-oriented workers (Lynn et al., 2011) and motivates them to provide more personalized service to their clientele (Kwortnik et al., 2009). Thus, eliminating tipping may reduce actual service levels. Further, consumers believe that tipping motivates servers to deliver better service (Mills and Riehle, 1987; Lynn and Wang, 2013), so eliminating tipping may reduce consumer expectations, and with them perceptions, of service quality and this could be the case even if actual service is unaffected. Kwortnik et al. (2009) research lends credence to the voluntary tipping-service quality link. The authors compared Zagat service ratings of Miami Beach restaurants and found that ratings were significantly higher in establishments with

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