The Effects of Tipping Policies on Customer Satisfaction:

A Test from the Cruise Industry

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ABSTRACT

Many in the media have called for the abolition of the practice of tipping and at least some resorts, private clubs, hotels, and restaurants have replaced tipping with automatic service charges or service inclusive pricing. Particularly notable in this regard is the cruise industry, where several of the largest brands have switched to an automatic service charge system. Given the popularity of tipping and its perceived role as an incentive/reward for service, such moves to replace tipping with service charges seem likely to have negative effects on customer satisfaction. We test this expectation by examining the effects of Carnival Cruise Line's tipping policy change in the early 2000s on its customers' evaluations of their cruise experience. After controlling for the effect of ship and review date, we found that Carnival Cruise Line's guests rated their cruise more positively when they sailed under a voluntary-tipping policy than when automatic service charges were added to their onboard bills. However, this effect was small and need not deter firms from replacing voluntary tipping with service charges. Discussion of this finding focuses on ways services marketers might be able to mitigate this modest negative effect of service charges.

KEY WORDS: tipping, service charges, customer satisfaction, cruise industry

In many sectors of the hospitality and tourism industry, servers receive voluntary payments of money—tips"—from customers as at least part of the compensation for their services. Consumers' decisions about whom and how to tip are largely determined by custom (Lynn, 2006). However, many in the media have begun to call for the abolition of this custom (Palmer, 2013; Peterson, 2013; Wells, 2013) and many resorts (Evans & Dave, 1999) and private clubs (Club Managers Association of America, 1996), as well as some hotels (Richards & Rosato, 1995) and restaurants (Wells, 2013) have replaced tipping with automatic service charges or service inclusive pricing. Particularly notable in this regard is the cruise industry. Prior to 1999, most cruise lines used a voluntary cash-based tipping policy, with only a handful of luxury lines using a no-tipping policy. However, by 2004, this picture had changed dramatically, with several of the largest cruise brands (e.g., Carnival Cruise Lines, Costa Cruise Lines, Cunard Line, Holland America Line, Norwegian Cruise Line, Oceania, and Princess Cruises) switching to an automatic service charge system (Engle, 2002).

One potential consequence of replacing tipping with automatic service charges, as a growing number of service firms are doing, is lower customer satisfaction. Such an effect may be produced by one or more of several processes. First, consumers prefer tipping to service charges (Lynn & Withiam, 2008), so replacing voluntary tipping with less popular service charges may directly lower customer satisfaction. Second, research indicates that consumers believe tips are incentives that improve service (Mills & Riehle, 1987), so replacing voluntary tipping with service charges may reduce expectations for service quality, which in turn affect perceptions of service through assimilation (Herr, Sherman & Fazio, 1983) and/or expectancy effects (Rosenthal & Rubin, 1978). Third, a series of studies by Kwortnik, Lynn and Ross (2009) found that voluntary tipping policies improve service levels by motivating servers to deliver friendlier and more personalized service, and a study by Lynn, Kwortnik and Sturman (2011) found that tipping helps to attract and retain more motivated and capable staff; taken together, these studies suggest that replacing voluntary tipping with service charges may reduce customer satisfaction by lowering actual service levels. With all of these theoretical processes pointing in the same direction, we hypothesize:

H1: Replacing tipping with service charges will reduce customer satisfaction.

Although there are strong theoretical reasons to expect moves away from tipping to reduce customer satisfaction, there are, to our knowledge, no empirical tests of this specific hypothesis. In this paper, we provide such a test. Specifically, we examine the effects of Carnival Cruise Lines' tipping policy change in the early 2000s on customers' evaluations of their cruise experience. Prior to 2001, Carnival Cruise Lines had a voluntary tipping policy. In 2001, however, Carnival began adding automatic daily service charges to passengers' bills instead. This change in tipping policy, which took about three years to roll out to all Carnival ships, was necessitated by Carnival's development of more onboard dining options, a service shift that it labeled, "Total Choice Dining." In addition to the greater variety of dining options, Carnival introduced reservations-only supper clubs as an alternative to evening meals in the main dining rooms. Since passengers were less likely to dine at the same table and be served by the same waiter for each meal, end-of-cruise tipping became less manageable and was replaced with the automatic service charge.[1] We examine passengers' overall ratings of their Carnival cruise from before and after the company's change in tipping policy in the study reported below.

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[1] Carnival, like several other cruise lines that moved to an automatic service charge system, allocates a percentage of guests' total service charge to dining staff. These tips are pooled and, therefore, do not reflect direct compensation for services rendered.

Method

<u>Sources of Data</u>

The data in this study come from several sources. A website—cruiseone.com—provided the voluntary ratings of Carnival cruises from 1,284 customers' between October 28, 1999 and July 20, 2004, along with the date the review was submitted. We selected this date range to capture the time period from roughly one and a half years before to one and half years after the change in tipping policies took place; we did not manipulate the selected date range to yield hypothesized effects. Carnival Cruise Lines was unable to provide us the exact dates that the tipping policies changed on each of their ships, so we searched online reviews and posted queries in on-line discussion boards from numerous websites to identify the ship, sailing date and tipping policy in place when reviewers and respondents to our queries took cruises on Carnival. By combining and comparing data from many different people and sources, we were able to obtain a date before which we are reasonably confident that specific Carnival ships had a voluntary tipping policy and a date after which we are confident the ships had an automatic service charge. The ships and before-and-after dates were:

- Destiny 6/01 11/01
- Ecstasy 5/02 12/02
- Elation 11/02 12/02
- Fascination 12/01 1/02
- Fantasy 7/01 10/01
- Imagination 4/01 8/02
- Inspiration 12/01 3/02
- Sensation 10/02 5/03

- Triumph 11/01 12/01
- Victory 1/02 6/02

Assuming that most of the reviews were posted shortly after the end of the cruise, cruises on each ship reviewed before the first date above were coded as occurring under voluntary tipping, while those reviewed one month after the second date above were coded as occurring under an automatic service charge. One hundred fifty-five reviews posted between these dates were not included in our study due to uncertainty about the tipping policy in effect on those sailings, resulting in a final sample of 1129.

Variables

The dependent variable in this study was reviewers' ratings of their overall cruise using a five-point scale with five being best. The primary independent variable was tip policy as determined above with automatic service charge coded as 0 and voluntary tipping coded as 1. In addition, ship (which was dummy coded) and the date the review was posted were used as control variables as well as potential moderators of tipping policy effects. Finally, the year each ship entered service (an inverse measure of ship age) and the total crew size (a measure of ship size) were obtained from Ward (2003) and used in tests of interactions with tipping policy.

Results

Descriptive statistics for the data in this study are presented in Table 1. A regression of cruise rating on ship, review date and tipping policy using robust standard errors produced significant effects for many of the ship dummy variables and a marginally significant positive effect of review date ($B = .0002$, $t(1117) = 1.43$, $p < .16$). More importantly, it produced a significant, positive effect of tipping policy ($B = .28$, $t(1117) = 1.77$, one-tailed $p < .04$). However, the effects of tipping on customer satisfaction were small with a partial r of .06 and an increase in estimated marginal means of only .28 (marginal means = 3.73 with no tipping vs 4.01 with tipping). Adding the product of tipping policy and each ship dummy to this regression model produced only one marginally significant interaction – the tipping policy effect was stronger for Fascination (the oldest ship in the sample) than for Victory (the youngest ship in the sample) ($B = .59$, $t(1108) = 1.68$, $p < .10$). However, given the large number of ships whose interactions with tipping policy were tested, this marginal interaction effect is probably due to chance. Additional analyses (testing each interaction term separately) found no reliable interactions of tipping policy with the date of the cruise ($B = -.000$, $t(1116) = -0.83$, n.s.), the size of the ship ($B = -.001$, $t(1116) = -0.95$, n.s.), or the newness of the ship ($B = -.02$, $t(1116) = -0.73$, n.s.).

Discussion

The results from this study show that after controlling for the effects of ship and review date, more than 1,100 Carnival Cruise Line guests rated their cruise more positively in the context of a voluntary-tipping policy than when automatic service charges were added to their onboard bill. The staggered introduction of service charges across Carnival's ships together with the statistical controls for ship and review data help to rule out most historical confounds. However, tipping policy was confounded with the introduction of more dining options on Carnival ships, and our controls do not account for this. Fortunately, "Total Choice Dining" was implemented in response to consumer preferences, so if anything, this confound should have weakened the effects of the voluntary tipping policy on cruise ratings. Thus, our findings support the idea that the move to replace voluntary tipping with automatic service charges entails some cost in terms of customer satisfaction.

The findings of this study do not necessarily mean the cruise industry and other hospitality firms employing service charges should return to voluntary tipping policies. An important caveat to our finding is that the size of the tipping policy effect, though statistically significant, was small. The effect size was a change of only about one-third of a rating point on a five point scale. The small size of this effect highlights the fact that satisfaction is influenced by myriad interacting factors above and beyond the role of tipping policy and indicates that high satisfaction levels can be achieved without tipping. [Note, however, that finding any effect of tip policy on customer satisfaction is remarkable given the length, complexity, and richness of the cruise experience. Tipping policies may have stronger effects in other service settings that are shorter and less all-encompassing than are cruises.]

Another caveat to our findings is that tipping policy effects on customer satisfaction may differ across customer segments. In particular, research indicates that tipping motivates servers to discriminate against those segments of customers thought to be poor tippers -- .e.g., ethnic minorities, the elderly, foreigners, etc… (Brewster, 2013, 2015; McCall and Lynn, 2009). This suggests that eliminating tipping may increase rather than decrease customer satisfaction among members of those discriminated against segments. Thus, the tipping policy effects in this study may not generalize to firms with large numbers of customers who are ethnic minorities, elderly, and/or foreigners.

In light of the aforementioned issues, the automatic service charge model emerges as a workable, though not yet optimal, policy. From a marketing-management perspective, optimizing the effects of an automatic service charge policy requires improving customer attitudes toward it and enhancing its role as an incentive for good service. Although we are going well beyond the data at hand, one means to accomplish these goals may be to facilitate customers' ability to vary the service charge within specified parameters to reflect their perceptions of service quality. At Carnival, adjusting service charge was possible, but could be inconvenient, as it required a personal visit to the purser's desk to make the request. Further, because most guests do not see their folio until the last day of the cruise, this often would lead to several hundred passengers converging on the purser's desk, along with other passengers needing to question or settle their accounts. The purser's staff would also question guests about their reasons for the adjustment, either for service recovery should the guest be dissatisfied with their experience or to reduce incidence of guests who simply do not want to pay a gratuity. As a result of these factors, the vast majority of passengers simply pay the service charge.[2] Making it easier to adjust the charge by enabling an adjustment via telephone, in writing, or electronically (assuming that electronic access to the guest folio can be made available, similar to the in-room check-out systems used in the hotel industry) might go a long way to reducing customer dissatisfaction with the charge and to convincing staff that they can still increase their earnings by delivering better service. Complementing this process modification should be enhanced communication with and training of the customer (and travel agent) to explain the automatic service charge system and reinforce the idea that it is an optional gratuity (a "reverse tip") and not a mandatory fee.

In addition to this external marketing, companies that use an automatic-service charge policy should focus on internal marketing (see Zeithaml & Bitner, 2003, p. 319) to help service workers to "…deliver on the service promise." With a reduced co-variation of compensation with delivered service in the automatic-service charge context, less motivated service workers

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[2] Carnival Cruise Lines estimated that one in seven guests ask to adjust the automatic gratuity, with most guests saying that they would prefer to tip in cash – though only half actually do. Approximately 6% of those guests who adjust the gratuity choose to add to the tip amount. This information was gathered via a phone interview with executives from Carnival's hotel department, September 21, 2004.

will likely discern the minimum level of effort required before customers choose to take the extra step of adjusting the service charge down. Likewise, there is less of an incentive to exert the extra effort and emotional energy (Katzenbach & Santamaria, 1999) needed to provide exemplary service, because so few customers adjust the service charge up. To counter this normalization in service effort wrought by lessened extrinsic rewards, it becomes more important to recruit workers who exhibit high levels of service aspiration, to reinforce through training and intrinsically-focused motivators (e.g., recognition rewards and job promotions) the importance of service professionalism, and to create a service environment that enables the delivery of service excellence (e.g., by fostering a service culture, by providing the right tools and technology, and by setting reasonable, obtainable service goals). In sum, service-marketing management should strive to shape both the customers' and employees' perception of the automatic service charge as a convenient form of optional tipping, as well as the reality of the system and how it is implemented as an incentive for good service.

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Table 1. Descriptive statistics for the variables in this study

	N	Minimum	Maximum	Mean	Std. Deviation
Satisfaction Rating	1129	1.00	5.00	3.84	1.17
Tipping Policy (0 = no tipping, 1 = tipping)	1129	.00	1.00	.40	.49
Destiny (0=no, 1=yes)	1129	.00	1.00	.12	.32
Ecstacy (0=no, 1=yes)	1129	.00	1.00	.06	.24
Elation (0=no, 1=yes)	1129	.00	1.00	.05	.22
Fascination (0=no, 1=yes)	1129	.00	1.00	.11	.31
Fantasy (0=no, 1=yes)	1129	.00	1.00	.11	.31
Imagination (0=no, 1=yes)	1129	.00	1.00	.07	.26
Inspiration (0=no, 1=yes)	1129	.00	1.00	.06	.24
Sensation (0=no, 1=yes)	1129	.00	1.00	.11	.32
Triumph (0=no, 1=yes)	1129	.00	1.00	.19	.39
Victory (0=no, 1=yes)	1129	.00	1.00	.12	.32
Valid N (listwise)	1129				