

ASSESSING CORPORATE SOCIAL RESPONSIBILITY IN HOSPITALITY ORGANIZATIONS USING LAWSUITS AS A GAUGE

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This study identifies and describes major lawsuits against Fortune 500 hotel, foodservice, and casino corporations over the past ten years and suggests that these suits are one indicator of Corporate Social Responsibility (CSR). Lawsuits claiming fraud, discrimination, unjust enrichment, copyright infringement, and wrongful death which ended in settlements or jury awards above \$2 million are included. This research follows the methodology of a 2006 study which examined similar claims against Fortune 100 companies.

KEYWORDS: *Corporate social responsibility, hospitality lawsuits, ethics*

In the early to mid-part of the last decade, it seemed as if claims of major corporate misconduct were occurring almost weekly. Successful companies including WorldCom and Enron filed for bankruptcy due to the fraudulent activities of their corporate leaders. High profile Chief Executive Officers including Dennis Koslowski of Tyco International and John Rigas of Adelphia Communications were convicted of a variety of crimes. The reputations of major corporations were tainted and stock values plummeted.

This era was filled with ethical and legal misdeeds, and brought the need for increased Corporate Social Responsibility (CSR) to the forefront. Corporate Social Responsibility, often called corporate conscience, mandates self-regulation and accountability to all current and potential stakeholders. Research into the practices and economic impact of CSR has been surfacing in a number of fields, but little has been done in the hospitality arena. A recent study examined social responsibility patterns in the top ten hotel companies (Holcomb et al., 2007). The socially responsible behaviors included in this study were self-reported on websites and in annual and CSR reports, and focused primarily on philanthropic and diversity initiatives. Similarly, an exploratory study was undertaken which examined self-reported philanthropic initiatives undertaken by lodging properties throughout the United States in an attempt to quantify the “social” aspect of CSR (McGehee, 2009).

The concept of CSR is broader though and also encompasses economic, ethical, and legal corporate behaviors (Carroll, 1991). Many describe law as “codified ethics” or, conversely, describe ethics as “legal compliance plus.” Thus, one way to study CSR patterns within the ethical and legal context is to categorically examine recent lawsuits and their outcomes.

A recent study found that forty corporations listed in the 1999 *Fortune 100* were considered “unethical,” defined as engaging in fraud (accounting, securities, or consumer), discriminatory practices, undisclosed executive pay, antitrust activities, patent infringement, or other violations of the law (Clement, 2006). The most frequent type of misconduct resulting in decisions, settlements, or fines of greater than \$2 million was accounting fraud (20 firms), followed by securities fraud (13 firms), consumer fraud (11

firms), discriminatory practices (six firms), antitrust activities (four firms), undisclosed executive pay (two firms), patent infringement (two firms), and other violations of the law (three firms). The most egregious violations occurred in the insurance and financial services industries, and none of the forty firms were primarily engaged in the hospitality industry.

Clement also recognized that a company that settles a lawsuit before it goes to court is not necessarily admitting a wrong. Rather, settling out of court may be in the best economic interest of the company in that the settlement may cost less than litigation. It is also important to note that larger corporations are statistically vulnerable to more lawsuits, and that current public interest, at any point in time, often results in an increased number of associated lawsuits.

This study follows Clement's methodology and focuses on two major segments of the hospitality industry from the 2010 *Fortune 500*: 1) Food Services and 2) Hotels, Casinos, and Resorts. The *Fortune 500* was used rather than the *Fortune 100* in order to capture hospitality firms to include in the study. Suits decided or settled between 2001 and 2010 will be included, expanding the study from Clement's five years to ten years. Finally, settlements and awards under \$2 million will generally not be mentioned. To date, no comprehensive study has focused on lawsuits filed against leading hospitality firms as an indicator of CSR. Thus, the major purpose of this study is to identify and describe major lawsuits and their outcomes as they relate to the ethical and legal parameters of CSR. The results of this study will necessarily be limited since relatively few hospitality firms are included in the *Fortune 500* and the number of lawsuits will be

less. However, this study will demonstrate the need to categorically examine lawsuits as they relate to the most flagrant violations of ethics and law which are both pillars of CSR.

Corporate Classification Methodology

Out of the 2010 *Fortune 500* list, ten companies were classified in the “food service” or “hotel, casino, and resort” category (*Fortune 500*, 2010). The companies, shown in Tables 1 and 2, include four in the food service industry and six in the hotels, casinos, and resorts industry, respectively, and are listed in order of their *Fortune 500* rank.

Table 1

Food Service Companies Included in the 2010 Fortune 500

Corporation	Revenue (\$ million)	<i>Fortune 500</i> Rank
McDonald’s	22,744.7	108
Yum! Brands	10,836.0	216
Starbucks	9,774.6	241
Darden Restaurants	7,217.5	311

Table 2

Hotel, Casino, and Resort Companies Included in the 2010 Fortune 500

Corporation	Revenue (\$ million)	<i>Fortune 500</i> Rank
Marriott International	10,908.0	213
Harrah’s Entertainment (aka Caesars Entertainment Corporation as of 11/10)	8,907.4	264
MGM Mirage	5,978.6	360
Starwood Hotels and Resorts	4,712.0	438
Las Vegas Sands	4,563.1	456
Host Hotels and Resorts	4,216.0	492

A study of lawsuits and statutory violations from 2001 through 2010 for each of these companies was conducted online through the *Wall Street Journal*, *The New York Times*, and Lexis/Nexis databases. As well, general search terms including the company's name, "lawsuit," and "million" were used. The searches were conducted numerous times using different search engines to best ensure that the major lawsuits and statutory violations were captured.

Lawsuits that were both litigated and settled out of court as well as suits which are under appeal are included. None of these searches revealed any incidences of undisclosed executive pay, antitrust violations, or patent infringements by any of the ten hospitality companies included in this study. However, some of these companies were unsuccessful defendants in lawsuits claiming unjust business enrichment, copyright infringement, and wrongful death. Each of these lawsuits and their outcomes will be discussed separately.

Accounting, Securities, and Consumer Lawsuits Claiming Fraud

While the hospitality industry has had its share of lawsuits, none were as monumental as those faced by the financial services and telecommunications industries during the past decade. In fact, over the past ten years, only five lawsuits filed against major hospitality firms claiming accounting, securities, or consumer fraud resulted in an out-of-court settlement or jury award of \$2 million or more. The \$2 million minimum threshold, in line with that used in Clement's study, generally excluded lawsuits which solely resulted in compensatory-based awards or settlements. meaning that the plaintiff was awarded back pay, lost benefits, and such. Rather, the \$2 million mark most often

included both compensatory and punitive damages, meant to simultaneously make the plaintiff “whole” while “punishing” the defendant.

When analyzing the lawsuits pertaining to the financial settlement or damages, a natural break was clearly apparent. Many suits fell into the aforementioned target categories, but were settled or adjudicated in the \$500,000 range. The damages in these suits were normally compensatory, meaning that the plaintiff was awarded back pay, lost benefits, and such. The \$2 million dollar minimum used in this study captured major settlements and judgments, many of which carried with them punitive damages in addition to compensatory damages, hence, the higher settlement or adjudicated amount. These settlements and awards ranged from \$2 million to \$12.5 million. The figures, though, pale in comparison to Clement’s findings of forty-four fraud-related lawsuits filed against *Fortune 100* companies from 2000 to 2005, some of which resulted in awards or settlements of \$1 billion or more (Clement, 2006).

It is worth mentioning though that, early last decade, five major hotel firms including Marriott and Starwood settled class action lawsuits in which plaintiffs claimed they were charged undisclosed fees in the form of “energy surcharges.” These suits were settled out of court, often requiring the hotel company to issue a \$10 voucher for a future stay (Stellin, 2003). Certain food service companies faced similar lawsuits including Pizza Hut and its parent company, Yum! Brands. The dollar amount of the potential settlement of these suits, though, was much higher than the actual payout amounts since not all plaintiffs chose to redeem their vouchers. None of these lawsuits will be included since the actual dollar amount of these settlements to date has not been determined.

The casino segment has also faced its share of recent lawsuits and these bear mentioning. A number of investors filed suits against Las Vegas Sands Corporation's CEO Sheldon Adelson and Board members in the Nevada state court claiming that securities fraud and mismanagement were responsible for the huge decline in stock values, but the suits were dismissed in November 2009 (Green, 2009). Two similar lawsuits filed in federal court in 2010 have not yet been decided or settled (Green, 2010). Six separate lawsuits against MGM Mirage claiming securities fraud were recently granted class action status, but have also not yet been decided or settled (*Lowinger v. MGM Mirage*, 2009). Neither of these pending class action suits will be included in the table below since both are requesting unspecified compensatory damages which cannot be quantified for the purpose of this study.

The much-publicized class action suit filed by Hindus and vegetarians against McDonald Corporation's undisclosed use of beef tallow in the production of their French fries resulted in the highest settlement or award in this category. The settlement required McDonald's to donate \$10 million to vegetarian, Hindu and/or Sikh, children's hunger relief, and Jewish charitable organizations. As well, they agreed to write a letter of apology to the affected groups and to establish an advisory board charged with making dietary recommendations to the corporation (*Block, Sharma, and Singh v. McDonald's*, 2001). In addition, McDonald's agreed to pay plaintiffs' attorney fees and to pay \$4,000 to each of the eleven plaintiffs.

Table 3**Major Lawsuits Claiming Accounting, Securities, and Consumer Fraud**

Company	Year	Nature of Misdeed	Description	Award/Settlement Amount
McDonald's Corporation	2002	Consumer fraud	Class action suit filed by vegetarians and Hindus claiming McDonald's deliberately misled customers by failing to disclose the use of beef tallow in the production of French fries (<i>Block, Sharma, and Singh v. McDonald's</i> , 2001)	\$12.5 million settlement
McDonald's Corporation	2005	Consumer fraud	Plaintiffs claimed McDonald's did not lower the amount of trans fat in their cooking oil after promising that they would (<i>Fettke v. McDonald's Corp.</i> , 2003)	\$8.5 million settlement
Harrah's Entertainment	2010	False advertising	Class action suit claimed the timing for the use of birthday club vouchers was misleading (<i>Smerling v. Harrah's Entertainment, Inc.</i> , 2006)	\$8 million jury award
McDonald's Corporation	2003	Fraud, recession of a release, and unfair business practices	Plaintiff, a long-time multiple franchisee, claimed she was wrongfully forced out of the system (<i>Darling v. McDonald's Corp.</i> , 2006)	Initial \$16.5 million jury award; \$10 million in punitive damages overturned on appeal; settled for remainder
Marriott International	2003	Antitrust violation	Suit filed by In Town Hotels claiming mismanagement, fraud, overcharging for services, and commercial bribery (<i>In Town Limited Partnership v. Marriott International, Inc.</i> , 2002)	\$2 million settlement

A number of obesity-related lawsuits filed against McDonald's followed this settlement and were dismissed on a variety of grounds. Similarly, a number of lawsuits were filed claiming that McDonald's French fries contained gluten although

McDonald's claimed they did not (*In re McDonald's French Fries Litig.*, 2009). The gluten-related suits were denied class action status in 2009 due to a district court judge's explanation that "individual issues of law clearly predominate over common issues, making a nationwide class unmanageable". To date, none of these claims has proceeded on an individual basis.

The increased public attention to the use of trans fats in cooking led to two other well-publicized lawsuits filed against McDonald's and Yum! Brands, the parent company of KFC. McDonald's settled their suit, filed by watchdog group BanTransFat.com and another plaintiff, for \$8.5 million in 2006. The American Heart Association received \$7 million of the settlement and the remaining \$1.5 million was used to fund a public education initiative about the potential dangers of trans fats ("*McDonald's Settles*," 2005). In 2006, the Center for Science in the Public Interest, another watchdog group, filed a similar lawsuit against KFC, but the suit was dropped in 2007 when KFC voluntarily stopped frying their chicken in oil with trans fats ("*CSPI Withdraws*, 2006).

The third case involved a false advertising and truth-in-advertising class action suit filed against Harrah's Entertainment in 2010. Harrah's gave away \$15 vouchers as part of their customer loyalty program, but unreasonably restricted the hours in which the vouchers could be redeemed. A jury awarded the 80,000 class action members \$100 each in statutory damages for a total of \$8 million (Parry, 2010).

In the fourth case, a long-time franchisee filed suit against McDonald's Corporation claiming fraud, recession of a release, and unfair business practices. The franchisee openly criticized some of McDonald's policies as they pertained to franchise requirements, and claimed that she was "forced out of the system." A jury awarded the

plaintiff \$16.5 million of which \$10 million was punitive (Edison, 2007). Upon appeal, the \$10 million in punitive damages was overturned and, upon the plaintiff's death, her estate settled out of court with McDonald's for the remainder (Kirkland and Ellis LLP).

The last lawsuit included in Table 3 was filed by In Town Hotels against Marriott International and claimed mismanagement and overcharging for services. In Town also challenged Marriott's vertical ties with Avendra, a procurement services company that is half-owned by Marriott. The suit was settled in 2003 when Marriott agreed to forego \$2 million in fees owed by In Town from the Charleston Marriott Town Center property (Browning, 2008).

Discrimination Lawsuits

The leading hospitality companies in this study fared well as compared to those in Clément's study regarding discrimination-based lawsuits. Since 2008, though, twenty-eight lawsuits claiming sexual harassment were filed against Harrah's Atlantic City, part of Harrah's Entertainment (Dunn, 2010). The plaintiffs are seeking injunctive relief and punitive damages. All of these suits are still pending.

Another case worth mentioning was filed in 2002 by celebrity chef Timothy Dean against the St. Regis Washington Hotel in Washington, D.C. The plaintiff claimed racial discrimination in that Marriott's management team tried to force him out of business and harassed him due to his race (Shiver, 2005). The \$50 million lawsuit was settled out of court for an undisclosed amount.

There were many other relatively high-profile suits filed claiming discrimination based on race, religion, national origin, gender, and sexual orientation, but in many cases,

they were settled out of court. In suits that went before a jury, the awards were less than the \$2 million threshold of this study.

Undisclosed Executive Pay

While no incidences of undisclosed executive pay per se were revealed, *The New York Times* reported that Chairman, Chief Executive, and Treasurer of the Las Vegas Sands, Sheldon G. Adelson, received \$3.6 million in salary and bonuses in 2005 due to “improper interpretation” of his employment contract. This was almost \$1 million more than he was entitled to had the contract been interpreted correctly (Morgenson, 2006). An additional \$1.8 million was awarded to four other top executives at the Las Vegas Sands due to the same “misinterpretation.” The Compensation Committee of the Sands admitted the error, but let all five executives keep the excess bonus payments based on “the outstanding performance of the company in 2005.”

Other Notable Lawsuits

The two lawsuits listed in Table 4 were included since each has a direct bearing on CSR as it pertains to both law and ethics. The settlement or award in each case was above the \$2 million threshold as well, and involved intellectual property rights and unjust enrichment claims.

Table 4***Other Lawsuits***

Company	Year	Nature of Misdeed	Description	Award/Settlement Amount
Las Vegas Sands	2009	Unjust business enrichment	Suit filed by three individuals who claimed they were key in helping the Las Vegas Sands secure a gambling license in Macau (Stutz, 2009)	\$42.5 million settlement
Yum! Brands	2001	Breach of implied contract and copyright infringement	Plaintiffs filed suit claiming that Taco Bell modeled its popular icon after their "Psycho Chihuahua" cartoon character (<i>Wrench LLC v. Taco Bell Corp.</i> , 1999)	\$41.9 million upheld on appeal

The first lawsuit was filed by three individuals who claimed that they were integral in assisting the Las Vegas Sands to obtain a Macau gambling license. Such licenses are notoriously difficult to acquire. In 2009, the Las Vegas Sands paid \$42.5 million to settle the suit. The Sands still faces a possible new trial in a suit filed by another individual who also claimed he assisted in the Sand's acquisition of the gambling license. The plaintiff in this case is seeking \$58.6 million in damages. A lower court in Nevada initially ruled in favor of the plaintiff, but was overturned by the state's supreme court which ruled that "a district judge shouldn't have admitted a hearsay statement during the trial: (O'Keefe, 2010). Since this ruling was procedural rather than substantive, it is likely that the suit will be refiled.

The second suit was highly publicized and involved the creative ownership of a talking Chihuahua that catapulted the brand image of Taco Bell. Two plaintiffs asserted copyright infringement and breach of contract. They claimed to have developed the "Psycho Chihuahua" cartoon character which was then transformed by Taco Bell into the

live Chihuahua which became a national icon. The five-year court battle ended in a \$41.9 million verdict for the plaintiffs.

Discussion and Further Research

This study was not designed to be exhaustive and in many ways is limited. The number of lawsuits filed against these hospitality companies regarding a key area of CSR was far fewer and the settlements and jury awards were markedly less than those identified in Clement's study. However, the sample size is only one-tenth of the size of Clement's sample and the number of lawsuits resulting in awards exceeding \$2 million is small. Nevertheless, the results seem to indicate that using qualified lawsuits as one indicator of CSR is a useful measurement tool because it objectively ferrets out the most egregious examples of disregard for ethical and legal principles. As well, the study establishes the effectiveness of its methodology in identifying significant awards.

A more conclusive examination of the ethical and legal profile of the hospitality industry would require a significantly broader study. Such a study should expand the definition of the industry, perhaps including segments such as airlines and entertainment, as well as extending the scope of the examination to the *Fortune 1000* instead of the *Fortune 500*. It might also be revealing if certain industry segments could be identified as experiencing higher rates of litigation pertaining to CSR. An investigation of actions initiated by the Securities and Exchange Commission could also be included. Finally, loosening some of the qualifying parameters, such as the amount of awards or settlements, might cast a wider net and permit more detailed study of the types of firms involved.

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