

# MINIMUM WAGE 101

July 2016

The debate over whether to raise the minimum wage has historically broken down between the hard reality of market economics and the more forgiving interests of social goals.

## WHAT IS THE MINIMUM WAGE?

The minimum wage is the starting hourly wage an employer can pay an employee for work. Currently, the federal minimum wage is \$7.25 an hour (part of the Fair Labor Standards Act). Some states and cities have raised their minimum wage higher than that. In most instances, the higher of the prevailing minimum wage requirements is binding for employers.

California and Massachusetts currently have the highest state minimum wages at \$10 per hour. Emeryville, CA, currently has the highest city minimum wage at \$14.82 an hour.

## WHO EARNS THE MINIMUM WAGE?

A 2015 report from the Bureau of Labor Statistic finds that almost half (48.2 percent) of all employees earning the federal minimum wage are between the ages of 16 to 24.<sup>1</sup>

Percent of Minimum Wage Workers By Age

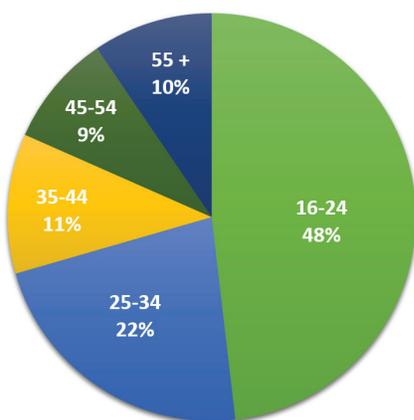


Figure 1. Percentage of Minimum Wage Workers by Age Range

Proponents of a higher minimum wage often describe the age distribution of the minimum wage workforce using the

proposed higher figure (e.g. \$10.10, \$12, or \$15) instead of the current minimum wage. This has the effect of raising both the average and median age of a minimum wage worker.

Even among these older groups, the “typical” minimum wage beneficiary doesn’t fit certain popular perceptions. Using Congressional Budget Office methodology, economists of Miami and Trinity University found that just one in 10 of those affected by a \$12 minimum wage are single parents with children. A majority of those affected are either second or third-earners in households where the average family income exceeds \$50,000 per year.<sup>2</sup>

Family Situation of Those Affected by a \$12 Minimum Wage

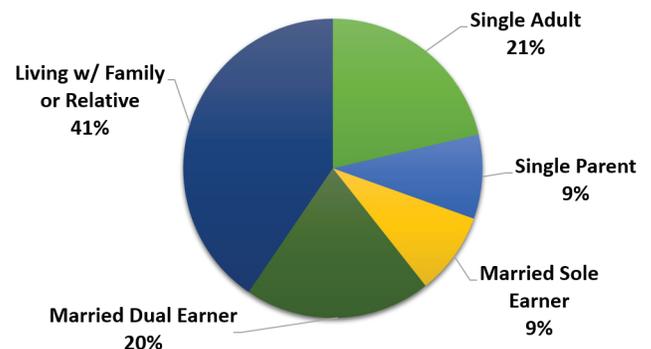


Figure 2. Family situation of those affected by \$12

## DO HIGHER MINIMUM WAGES LEAD TO JOB LOSS?

Proponents say that boosting the minimum wage will reduce poverty without reducing jobs. But the best and most credible academic evidence shows otherwise: According to a 2007 summary of the minimum wage research authored by economists at the Federal Reserve Board and the University of California-Irvine, roughly 85 percent of the best research from the past two decades shows that a higher minimum wage reduces employment.<sup>3</sup>

A December 2015 report from the Federal Reserve Bank of San Francisco incorporated the most-current research,

<sup>1</sup>U.S. Bureau of Labor Statistics. Characteristics of Minimum Wage Workers, 2014. 2015. <http://www.bls.gov/opub/reports/minimum-wage/archive/characteristics-of-minimum-wage-workers-2014.pdf>.

<sup>2</sup>Macpherson, D., Dr., & Even, W., Dr. “The Effects of a \$12 Federal Minimum Wage.” Employment Policies Institute, March 2016.

<sup>3</sup>Neumark, David, and William L. Wascher. “The Effects of Minimum Wages on Employment.” Minimum Wages, 2008, 36-106. doi:10.7551/mitpress/9780262141024.003.0003.

and concluded that, “[The] overall body of recent evidence suggests that the most credible conclusion is a higher minimum wage results in some job loss for the least-skilled workers...”<sup>4</sup> According to the non-partisan Congressional Budget Office, a \$9 national minimum wage would cost 100,000 jobs; a \$10.10 minimum wage would cost a half-million jobs.<sup>5</sup> And according to a follow-up analysis using the CBO methodology, a \$12 minimum wage would destroy 770,000 jobs.<sup>6</sup>



Figure 3. CBO Estimates of Job Loss from Each Wage Increase

## HOW ARE EMPLOYERS ADJUSTING TO HIGHER MINIMUM WAGES?

Employers who utilize minimum wage labor typically operate on razor-thin profit margins. Raising labor costs forces these businesses to either raise prices, reduce employee job opportunities, or cut some of the services that they provide.

Perhaps the fastest growing consequence of a higher wage is the expedited shift to automation – replacing low-wage workers with technology. Andy Puzder, the CEO of Carl’s Jr., explained, “If you’re making labor more expensive, and automation less expensive — this is not rocket science.”<sup>7</sup>

In the past decade, we’ve seen Blockbuster replaced by Redbox and Netflix, parking and toll road attendants traded for self-service machines, rapid growth in the availability of self-service checkouts, and airport ticket agents working side by side with full-service check-in kiosks.

McDonald’s has already installed over 7,000 self-service kiosks in higher-cost European markets. They’ve also been experimenting with kiosks in the US, and recently began

testing McCafe coffee kiosks in Chicago. Recently, Wendy’s announced their plan to replace employees with self-service kiosks, and numerous other restaurants have done the same.

Automation is not a new concept; self-service gas stations became a reality in the mid-70’s. Artificially inflating labor costs will only hasten employers decisions to automate.

## WHAT DO MOST ECONOMISTS THINK ABOUT \$15?

A recent survey conducted by the University of New Hampshire Survey Center finds that nearly three-quarters of surveyed US-based economists oppose a federal minimum wage of \$15.00 per hour. The majority believe a wage hike of this magnitude will have negative effects on youth employment levels (83 percent), adult employment levels (52 percent), and the number of jobs available (76 percent).

Prominent liberal economists who support a higher wage, including alumni of the Obama and Clinton administrations, oppose a federal wage hike of this magnitude.

The University of New Hampshire survey also finds that at lower levels (under \$11.00 per hour) of proposed federal minimum wages, economists are divided largely by self-identified party identification as to an acceptable rate. The majority of Republicans and Independents who responded favoring lower minimum wages (\$7.50 per hour or less) and a number of Democrats who responded preferring a minimum wage between \$10.00 and \$10.50 per hour.

## DOES A STUDY OF FAST FOOD RESTAURANTS IN NEW JERSEY FIND THAT EMPLOYMENT INCREASES AS A RESULT OF A HIGHER MINIMUM WAGE?

In 1994, Princeton economists David Card and Alan Krueger looked at New Jersey’s fast-food restaurants in the wake of the state’s 1992 minimum-wage hike—and found that employment increased relative to similar restaurants in bordering Pennsylvania counties.<sup>8</sup> But six years later, the Card & Krueger study was refuted in the same economic journal that originally published it on account of serious data problems.<sup>9</sup>

<sup>4</sup>“The Effects of Minimum Wages on Employment.” Letter from Federal Reserve Bank of San Francisco

<sup>5</sup>Congressional Budget Office. The Effects of a Minimum-Wage Increase on Employment and Family Income. Report. 2014. [https://www.cbo.gov/sites/default/files/113th-congress-2013-2014/reports/44995-MinimumWage\\_OneColumn.pdf](https://www.cbo.gov/sites/default/files/113th-congress-2013-2014/reports/44995-MinimumWage_OneColumn.pdf)

<sup>6</sup>Macpherson, D., Dr., & Even, W., March 2016

<sup>7</sup>Taylor, Kate. “Fast-food CEO Says He’s Investing in Machines Because the Government Is Making It Difficult to Afford Employees.” Business Insider. March 16, 2016. <http://www.businessinsider.com/carls-jr-wants-open-automated-location-2016-3>.

<sup>8</sup>Card, David, and Alan Krueger. “Minimum Wages and Employment: A Case Study of the Fast Food Industry in New Jersey and Pennsylvania.” *The American Economic Review*, 1993. doi:10.3386/w4509.

<sup>9</sup>Neumark, David and William Wascher. 2000. “Minimum Wages and Employment: A Case Study of the Fast-Food Industry in New Jersey and Pennsylvania: Comment.” *American Economic Review*, 90(5):1362-1396.

The problem stemmed from, among other things, a failure to properly define terms like “full time” and “part time,” or what constituted a regular hamburger. Survey researchers collecting the data pre and post wage hike reported numbers that suggested implausible swings in food prices and employment in less than a year’s time. Note the significant discrepancies in the table below: In some cases, a “regular” hamburger nearly doubles in price—in an industry where even a five percent price increase would be difficult to sustain.

Table 1. Card-Krueger data on the price of a hamburger in every company-owned Wendy’s in Pennsylvania

Price of “Regular” Hamburger	
February	November
\$1.65	\$0.95
\$0.95	\$1.79
\$1.75	\$0.94
\$0.90	\$0.90
\$1.01	\$0.94
\$0.84	\$0.79
\$0.85	\$0.90

A subsequent study that relied on payroll records rather than telephone survey data confirmed that employment did indeed decline following the minimum wage increase in New Jersey.

## ARE THERE REAL STORIES THAT SUPPORT THE RESEARCH FINDINGS?

Examples of the unintended consequences that accompany a higher wage can be seen in the states and cities that have implemented significant wage hikes. Many stories can be found at [facesof15.com](http://facesof15.com). Several examples are outlined below.

In March of 2015 Berkeley, California raised its minimum wage by 36 percent, from \$9 to \$12.25. Mokka, a local coffee shop, tried a number of strategies to compensate for the additional labor costs including higher prices, new menu items, and offering alcohol. Ultimately the management decided not to renew their lease in 2016, citing the minimum wage hike as the deciding factor.

In December of 2015, New York instituted a \$2.50 an hour increase to the wages of tipped staff. Longway’s Diner in upstate New York has been an institution for truckers on the East Coast since 1966. Shortly after the wage hike they

## Average Inflation-Adjusted Minimum Wage Since 1938 is \$7.40

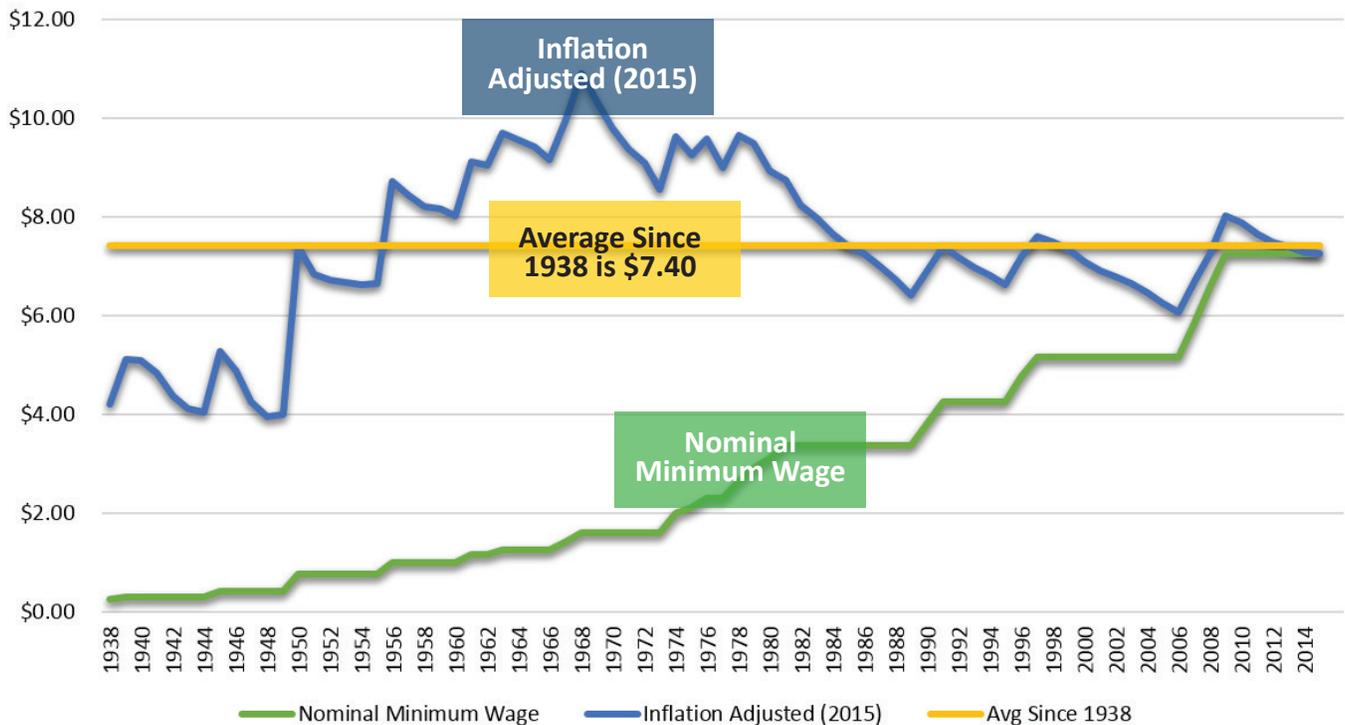


Figure 4. Nominal Vs. Inflation-Adjusted Minimum Wage Based on CPI Data, Since 1938

<sup>10</sup> Booker, T. “Restaurants cut staff hours after tipped wage hike”. NNYBizMag.com, January 07, 2016. <http://www.nnybizmag.com/index.php/2016/01/07/restaurants-cut-staff-hours-after-tipped-wage-hike/>

<sup>11</sup> Sabia, Joseph J., and Richard V. Burkhauser. “Minimum Wages and Poverty: Will a \$9.50 Federal Minimum Wage Really Help the Working Poor?” Southern Economic Journal 76, no. 3(2010):592-623. doi:10.4284/sej.2010.76.3.592.

<sup>12</sup> Congressional Budget Office. The Effects of a Minimum-Wage Increase on Employment and Family Income. Report. 2014.

announced that they will no longer be open 24/7. The owner—who inherited the diner from his late father – cut shifts in an effort to cover the extra costs from the additional labor costs.<sup>10</sup>

## DOES RAISING THE MINIMUM WAGE REDUCE POVERTY OR SPENDING ON GOVERNMENT ASSISTANCE?

Proponents of a higher wage often claim that a higher wage is necessary to eradicate poverty. Evidence suggests otherwise. Twenty-eight states raised their minimum wage between 2003 and 2007. Yet research from economists at Cornell and American University found no associated reduction in poverty.<sup>11</sup> One of the factors that the authors identify is poor targeting: Census Bureau data show that over 60 percent of the poor don't have a job, and thus can't benefit from a higher wage.<sup>12</sup>

Data from the Census Bureau's Current Population Survey was used to study the current working age population – 18 to 64-year-olds – living in poverty in each state. The analysis yields similar results; in 41 states and the District of Columbia, at least half of adults living in poverty are not employed and can't benefit from a "raise."

Another commonly-cited argument for raising the minimum wage is that it will reduce taxpayer spending on social programs. Dr. Joseph Sabia of San Diego State University and Thanh Tam Nguyen examined 35 years of government data across a number of different datasets and determined that, on net, minimum wage increases have little to no net effect on participation in—or spending on—a range of means-tested programs.<sup>13</sup>

## HAS INFLATION ERODED THE MINIMUM WAGE?

The vast majority of workers affected by minimum wage rates are employed in the service and retail industries. According to the 2015 Bureau of Labor Statistics report, the leisure and hospitality industry employs the largest amount of minimum wage earners.<sup>14</sup>

When the wage standard was first implemented in 1938, unskilled retail and service employees were not covered by the law. It was a minimum wage that covered mostly manufacturing, mining and transportation – it was a

minimum *skilled* wage. But as Congress expanded the reach of the minimum wage law, the standard became irrelevant to skilled workers and became the minimum *unskilled* wage.

Proponents often argue that if the minimum wage had tracked inflation it would be far greater than the current rate of \$7.25. But data from the Consumer Price Index, suggests that when adjusted for inflation the 1938 federal minimum wage of 25 cents would have been \$4.20 in 2015. The average inflation-adjusted value since 1938 is \$7.40 an hour—or just 15 cents more than the current federal minimum wage. (See Figure 4 on previous page)

## IF THE MINIMUM WAGE HAS SUBSTANTIAL DRAWBACKS, WHY ARE THE MAJORITY OF PEOPLE FOR IT?

A recent national poll commissioned by the Employment Policies Institute and conducted by ORC International (CNN's pollster) found that nearly six in ten Americans supported a higher minimum wage. But – like most popular polls on the issue – these results are incomplete.

When informed of the unintended consequences that accompany that higher mandated wage the results flipped. When respondents were informed that a \$15 minimum wage would cause some less-skilled employees to lose their jobs, 52 percent opposed the policy. The opposition grew to 63 percent when respondents were informed that a \$15 hourly minimum wage would cause some small businesses to close.

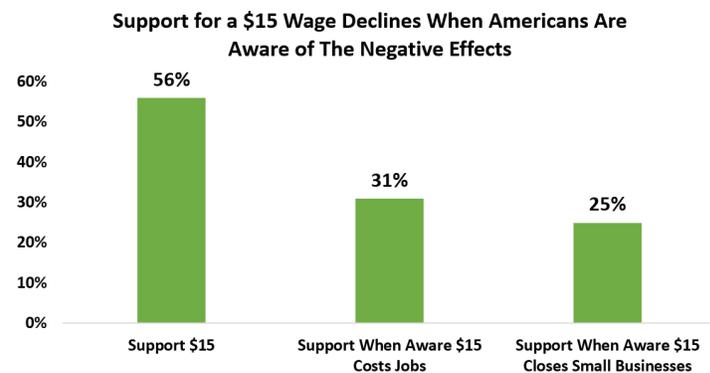


Figure 5. Survey Results for Support of \$15 Minimum Wage<sup>15</sup>

<sup>13</sup>Sabia, J. J., & Nguyen, T. T. The Effects of Minimum Wage Increases on Means-Tested Government Assistance. Report. December 2015. [https://www.epionline.org/wp-content/uploads/2016/01/EPI\\_MW\\_GovtAssist\\_Study\\_V2-5.pdf](https://www.epionline.org/wp-content/uploads/2016/01/EPI_MW_GovtAssist_Study_V2-5.pdf)

<sup>14</sup>U.S. Bureau of Labor Statistics. Characteristics of Minimum Wage Workers, 2014. 2015.

<sup>15</sup>ORC International. *Federal Minimum Wage Poll*. Employment Policies Institute, 2016.

<sup>16</sup>Baum, C. L., & Ruhm, C. J. The Lasting Benefits of Early Work Experience. Report. August 2014. [https://www.epionline.org/wp-content/uploads/2014/08/EPI\\_LastingBenefitsofEarlyWorkExperience2.pdf](https://www.epionline.org/wp-content/uploads/2014/08/EPI_LastingBenefitsofEarlyWorkExperience2.pdf)

<sup>17</sup>Mroz, T. A., Dr., & Savage, T. H., Dr. The Long-Term Effects of Youth Unemployment. Report. October 2001. [https://www.epionline.org/wp-content/studies/mroz\\_10-2001.pdf](https://www.epionline.org/wp-content/studies/mroz_10-2001.pdf)

## WHAT'S THE VALUE OF AN ENTRY LEVEL JOB?

Missing out on a job isn't just hard in the short term— it's detrimental to future career prospects for youth and the least skilled workers. Economists from the University of Virginia and Middle Tennessee State University found that young adults who worked part time in high school were earning 20 percent more six to nine years after graduation compared with their counterparts who didn't find part-time work while in school.<sup>16</sup> More troubling, an analysis from economists at Welch Consulting and the University of North Carolina found that teens who are unemployed today are more likely to be unemployed in the future.<sup>17</sup>

Economists tied this benefit to the career experience that's gained in an entry-level job — the “invisible curriculum” that teens pick up from reporting to a manager, interacting with customers and showing up to work on time. These are skills that teens don't pick up in high school and often don't have role models to mimic.

## WHAT ARE THE ALTERNATIVES TO RAISING THE MINIMUM WAGE?

While the empirical research suggests that a higher minimum wage is an ineffective means to reduce poverty, there are more efficient alternatives. The Earned Income Tax Credit (EITC) has a proven track record.

A recent survey conducted by the University of New Hampshire found that the majority of surveyed economists (71 percent) believe that the Earned Income Tax Credit (EITC) is a very efficient way to address the income needs of poor families. But only five percent believe a \$15.00 per hour minimum wage would be very efficient.

Economists Joseph Sabia at San Diego State University and Robert Nielsen at the University of Georgia found a 1 percent drop in state poverty rates associated with each 1 percent increase in a state's EITC. (The same study found no relationship between minimum wage hikes and poverty rates.)<sup>18</sup>

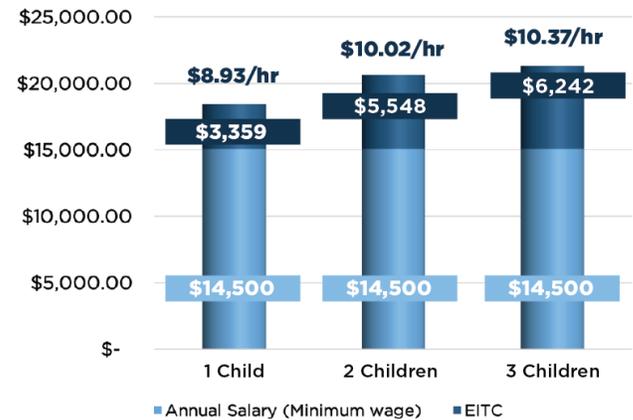
## HOW DOES THE EITC WORK?

By targeting recipients through the tax code, the EITC is able to supplement the income of low income households

without creating additional burdens on employers. The credit constitutes a fixed percentage of earnings for each dollar earned up until the credit reaches the maximum. An earners' maximum credit depends on several factors including earned income, marital status, and number of children.

The graph below illustrates the monetary impact the EITC has for a minimum wage worker who earns the federal minimum wage, depending on the number of children they have.

**Graph 1. EITC Benefit for a Single Minimum Wage Earner**



*Figure 6. Monetary Benefit of the EITC for a Federal Minimum Wage Earner<sup>19</sup>*

## IS IT TIME TO END TIPPING?

In high wage markets, some full-service employers have experimented with eliminating tipping. By abolishing tips in favor of a 20 percent (or more) price increase or service charge, the restaurateur can redistribute money that was previously restricted to serving staff to help fund raises elsewhere.

But often times tipped employees have more to lose under the tipless system. San Francisco restaurants Trou Normand and Bar Agricole estimated they lost 70 percent of their wait staff during a tip-free experiment in 2015, despite the higher salaries. Owner Thad Vogler told CNN Money that his servers in San Francisco were making as much as \$45 an hour with tips, and \$20 to \$35 an hour without.<sup>20</sup>

The Employment Policies Institute used Google's Consumer Survey tool to poll roughly 2,500 self-reported restaurant employees who earn tips, and nearly 60% rejected even a \$15 minimum wage if it meant they would no longer receive

<sup>18</sup>Nielsen, R., & Sabia, J. J. “Minimum Wage Increases Have Failed To Help Low-Income Americans Pay Rent, Meet Monthly Expenses.” Employment Policies Institute, April 2012. <https://www.epionline.org/release/o340/>.

<sup>19</sup>EITC Central. EITC December 2015 Calendar Year Report. June 2015. <https://www.eitc.irs.gov/EITC-Central/eitcstats>

<sup>20</sup>Vasel, Kathryn. “This Restaurant Killed Tipping...and Now It's Bringing It Back.” CNNMoney. January 19, 2016. <http://money.cnn.com/2016/01/19/pf/no-tipping-reversed-bar-agricole-trou-normand/>.

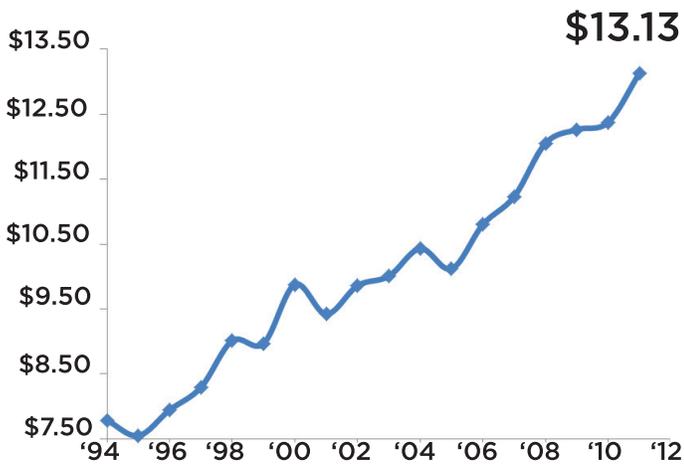
<sup>21</sup>Horizon Media, Inc. “Horizon Media Study Finds Most Consumers Not Ready to Stop Tipping.” Horizon Media Study Finds Most Consumers Not Ready to Stop Tipping. February 2, 2016. <http://www.prnewswire.com/news-releases/horizon-media-study-finds-most-consumers-not-ready-to-stop-tipping-300213406.html>.

tips. Most customers also favor the current tipping system. A recent survey of 3,000 U.S. consumers by Horizon Media found that a significant 81% prefer the status quo to a tip-free alternative.<sup>21</sup>

## IS THE TIPPING SYSTEM EXPLOITATIVE?

The tipping system is no different than a commission-based sales position. Tipped employees are guaranteed the same minimum wage as all other employees. And in reality, take-home wages for tipped employees are many times larger than their required hourly minimum. Census Bureau data show that tipped restaurant employees report earning over \$13 per hour and top earners bring in \$24 an hour of more.

Even in states where the base wage for tipped employees has been constant since the early 1990s, total take-home pay has increased in almost every year, as tip income has increased along with food and beverage prices.



Note: Census Bureau Current Population Survey Data, States Where Cash Wage Matches Federal.

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