CRY WOLF PROJECT

Minimum Wages
By Stephanie Luce
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The idea of minimum wage laws has been around for more than a century. As workers toiled in early factories, they fought for a floor wage that would allow them to meet their basic needs.

In the U.S., the first minimum wage law was passed in Massachusetts in 1912. A number of other states followed suit, and then in 1938, the federal government passed a minimum wage as part of the Fair Labor Standards Act (FLSA). That initial wage, set at 25 cents an hour, was not pegged to any formula but was rather a political compromise for those who opposed starting with a 40 cent an hour rate. The new law was not universal: lawmakers excluded certain workers from coverage - notably, agriculture and domestic workers. Over time there have been numerous revisions to the FLSA which have expanded coverage, though not all workers are entitled to the minimum wage, and workers who receive tips have a lower minimum wage rate.[1]

Many states still have their own state minimum wage laws. Some simply peg the state wage to the federal wage but may increase coverage, others have rates higher than the federal, and some have rates lower than the federal rate (which applies for those not covered by federal law). Five states have no state minimum wage law.[2]

More recently, some cities have passed their own citywide minimum wage laws. Whether a city has the authority to do this depends on state's homerule laws. Currently, there are citywide minimum wages in place in Washington DC; San Francisco, CA; and Albuquerque and Santa Fe, NM.

Currently, the federal minimum wage is not indexed to the cost of living, and only goes up with an Act of Congress. This differs from some other countries that have detailed formulas to determine the minimum wage on an annual basis. In recent years, minimum wage supporters have managed to get state minimum wage laws indexed to a cost of living formula in 10 states and one city.

Arguments for a Minimum Wage

Public opinion polls since the 1940s show that the majority of Americans support the minimum wage. Many people believe minimum wage laws are a way to make the labor market fair for low-wage workers who would not be able to bargain for higher wages on their own. Unions argue that setting a minimum wage will help take wages out of competition, meaning that firms are forced to compete on quality or innovation rather than by cutting wages.

Some of the early vocal supporters for a minimum wage came from clergy members. Father John Ryan, a Catholic priest, wrote a doctoral dissertation advocating for a minimum wage, which was published as a book in 1906. Ryan argued that

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[1] See the U.S. Department of Labor for more detail on which enterprises and workers are covered by the FLSA: http://www.dol.gov/whd/regs/compliance/hrg.htm#2

[2] For a list of state minimum wage rates and coverage, see http://www.dol.gov/whd/minwage/america.htm.

employers had a moral obligation to pay a wage high enough for a worker to support himself and his family.

Other advocates say that minimum wages can be good for the economy, in several ways. First, by raising wages for the lowest-wage workers you can assure that more money circulates in the economy. Low-wage workers tend to spend most of their earnings (rather than high-wage earners who might save money). This spending can have a multiplier effect, supporting local businesses that in turn may hire more workers. In addition, some economists suggest that paying higher wages can create “efficiency wage gains” - gains from lower turnover and absenteeism and higher productivity.

While there has always been general public support for raising the minimum wage there is not always a natural advocacy group or coalition that makes the issue a top priority. Over the years, support for higher minimum wages has come primarily from labor unions, community organizations, and some Democratic Party policymakers.

Arguments against the Minimum Wage

Those opposed to minimum wage legislation rely heavily on neoclassical economics for the content and evidence of their case. The primary argument is that when governments set wage floors, they interfere in free markets, and force wages above the market rate. By doing so, they create unemployment, as employers are forced to lay off workers. A Heritage Foundation article summed up the argument with this headline: “Econ 101: The Minimum Wage Kills Jobs” (Carroll 2010). Kevin Hassett (2006) of the American Enterprise Institute adds, “It is hardly rocket science. If you raise the price of apples, people buy fewer apples. If you raise the price of labor, firms buy less of it.” It isn’t just that employers can’t afford to pay a higher wage, but also that the worker is not worth it. Those who believe markets operate efficiently believe that the worker who had received a lower wage was receiving only the wage they are worth. To pay a worker a higher wage would be, according to economist Milton Friedman, “an act of charity” (Norman 1973). Therefore, employers will stop hiring the workers with fewer skills and qualifications - the very workers the minimum wage was intended to help.

But it isn’t just that employers cut jobs, say opponents. They are additional negative effects. According to Gregory Mankiw, former chair of the Presidents Council of Economic Advisors, raising minimum wages will entice teens to drop out of school to look for jobs (Mankiw 2001). Other researchers say that higher minimum wages are bad for teens and young adults because they are likely the first ones laid off when wages go up. In a *Wall Street Journal* op-ed economist David Neumark (2009), wrote “The best estimates from studies since the early 1990s suggest that the 11% minimum wage increase scheduled for this summer will lead to the loss of an additional 300,000 jobs among teens and young adults.” Others suggest that teens are really the only people earning minimum wage and that it’s a myth that adults try to support families on low wages. Tom Delay argued against the minimum wage increase in 1996, “Emotional appeals about working families trying to get by on $4.25 an hour are hard to resist. Fortunately, such families don't really exist.”

Similarly, studies done by the restaurant-industry funded Employment Policies Institute argue that minimum wage increases also lead to negative outcomes for minority workers. The author, David Neumark (2007), estimates that a 10 percent increase in the minimum wage will lead to a decrease in employment for African-Americans and Latinos, of 3.9 percent. In 1973 Milton Friedman told *Playboy Magazine*, “I’ve often said the minimum-wage rate is the most anti-Negro law on the books” (Norman 1973).

In addition to teens and people of color, opponents assert that small businesses are particularly harmed by minimum wages. Mark Alesse and Matthew Guilbault, members of the National Federation of Independent Business, argue, “A small increase of $1.60 per hour would cost a bake shop with ten clerks and bakers over $30,000 per year, not counting the increases that a higher payroll brings in the costs of workers compensation insurance, unemployment insurance, Social Security taxes, Medicare taxes and even liability insurance in some cases” (Alesse and Guilbault 2004).

Another argument used in the past is that raising minimum wages leads to inflation. If employers can not lay off workers, they will pass on the cost of the wage increase in the form of higher prices to consumers. While economists do not argue that minimum wage increases cause inflation, it is a common argument cited in newspaper reports and letters to the editor. A Seattle Post-Intelligencer article quoted a local business person’s opposition to a proposed increase: "If the minimum wage goes up with inflation, it also will cause inflation. It's like the Blob - it gets bigger and bigger” (Penhale 1998). Congressman Harris Fawell (R-IL) went so far as to claim **“**Economists from all persuasions agree that increasing the minimum wage will mean lost jobs and it will mean inflation.”

There is a host of other arguments against the minimum wage, including minimum wages increase job turnover (Hall 1982) to the minimum wage encourages employers to hire undocumented immigrants (Beranek 1982). One of the most common assertions in recent years is that the minimum wage is an inefficient way to help the poor, and that policies such as the Earned Income Tax Credit (EITC) are better tools that should be used instead of minimum wage laws.

In addition to arguments based on neoclassical economics, some opponents object to minimum wage laws on ideological grounds. Minimum wage laws are seen as an intrusion by government into free market contracts and the freedom of employers to pay the wage they want to pay. Representative Jeb Hensarling (R-TX) spoke out against a proposal to raise the federal minimum wage in 1997, suggesting that doing so would impede personal freedom: “Mr. Speaker, in America, we can either have maximum opportunity or we can have minimum wages. We cannot have both. In the land of the free, in a Nation as great as ours, how can we deny people their maximum opportunity, their opportunity to secure the American Dream?” Similarly, Representative Tom Hagedorn (R-MN) made this case:

> The question of the minimum wage goes beyond the immediate problem. It strikes at a basic underpinning of our democratic system. It touches on the ability of individuals to enter freely into contact without coercion and without arbitrary restrictions for mutual profit. Have we so soon forgotten that the American Revolution was fought in part because of such restrictions? Have we forgotten that there is a correlation between a free market economy and the amount of personal freedom enjoyed by the inhabitants of a country?

Finally, opponents argue that minimum wages are not really intended to help low-wage workers but to help labor unions or politicians. A Cato Institute brief argues, "Minimum-wage legislation is and always has been the result of special-interest politics. Behind the rhetoric of economic justice and fairness lie purely self-serving political considerations." In a *Wall Street Journal* article a management consultant had this to say about a politicians demand that the minimum wage be raised: "Political nonsense is rarely a sign of stupidity. It is more often a sign of opportunism" (Whyte 2010).

Minimum Wage Studies

There are hundreds of studies on the impacts of minimum wages, although many of these are built on econometric models that predict the impacts of minimum wage increases rather than empirical studies that use data to assess what actually did happen. A lot of the work also used methodological techniques that were not able to separate out the impacts of minimum wage increases from larger economic trends.[3]

In the 1980s, economist David Card created a splash within the field with his "natural experiments" that compared a treatment group (states with increased minimum wages) to a control group (states without an increase). Borrowing in part on earlier work by Richard Lester, Card (along with Alan Krueger and Lawrence Katz) attempted to advance the debates within economics with a series of studies looking at the statewide minimum wage increases of the late 1980s and early 1990s. Card and Krueger's best-known work analyzed the impact when New Jersey increased its statewide minimum wage in 1992, from $4.25 to $5.05 an hour. Card and Krueger looked at employment, wage and price data in fast-food restaurants along the New Jersey-Pennsylvania border, reasoning that any negative impacts would be likely seen in a low-wage intensive industry and where employers mandated to pay a higher wage in New Jersey would have to compete with their counterparts just across the state line. They surveyed about 400 restaurants just before the minimum wage went into effect, and then again eight months later.

To the surprise of many economists, Card and Krueger found no negative employment effects in their New Jersey study or in any of their other case studies. The finding was a surprise because theory and modeling predicted the opposite outcome. Immediately, Card and Krueger were attacked by Richard Berman of the Employment Policies Institute, a policy lobbying group funded by the restaurant industry.[4] Berman called Card and Krueger's work flawed. From there, a full debate ensued in the academic literature and the news media. Berman asserted that the work of David Neumark and William Wascher, which utilized restaurant industry payroll data, was more accurate, and that their work did find disemployment effects. It turned out, however, that the payroll data Neumark and Wascher used was supplied by the Employment Policies Institute, and Neumark and Wascher's results did not actually differ much from Card and Krueger's results.

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[3] Liana Fox (2006) provides a useful summary of minimum wage research methodologies and findings.
[4] The Employment Policies Institute is a D.C. based organization that is a vocal critic of minimum wage laws. It is not to be confused with the Economic Policies Institute, another D.C. based organization that generally favors increases in the minimum wage.

Similarly, economists have presented dueling studies on the impact of a citywide minimum wage increase in Santa Fe, New Mexico. Aaron Yelowitz used Current Population Survey data to estimate the impact of the $8.50 an hour minimum wage implemented in Santa Fe in 2004. In a study also published by the Employment Policies Institute, Yelowitz concluded that the new minimum wage led to an increase of 3.2 percent in the city unemployment rate (Yelowitz 2005). Economists at the University of Massachusetts-Amherst used the same data as Yelowitz and tried to replicate his results but could not do do. They found no evidence of job loss, and concluded that Yelowitz achieved his results "through a presentation of evidence that is misleading and incomplete, misusing the available data" (Wicks-Lim and Pollin 2005).

Researchers have conducted a series of empirical studies of minimum wage increases in Florida, Oregon, Washington, Wisconsin and the city of San Francisco have not found negative outcomes associated with the legislation. Recent work by Dube, Lester and Reich (2010) examined minimum wage differences in contiguous counties along state borders, for the 1990 and 2006. They find no evidence that higher minimum wages leads to job loss. Research by Allegretto, Dube and Reich (2010) finds that previous studies of teen employment failed to take into account strong variations in patterns of teen employment including geographic differences. Once these factors are controlled for, there is no impact from minimum wage increases on teen employment.

Economists continue to study the impact of minimum wage increases. Some still argue that minimum wage increases have negative impacts for certain populations, particularly teens, but most economists now acknowledge that disemployment effects, if they exist, are small. In 1993, economists and minimum wage opponents Richard Burkhauser and T. Aldrich Finegan wrote in a Cato Institute journal, "Over four decades of empirical studies leave no doubt that increases in the minimum wage do reduce employment to some extent. Yet by most counts, the number of lost jobs is trivial in the aggregate."[5] In 2006, over 650 economists, including five Nobel Prize winners, called on Congress to raise the federal minimum wage, stating that a modest increase in the wage would be beneficial for low-wage workers and the economy as a whole.

Also in 2006, a Wells Fargo-Gallup Small Business Index poll of small business owners and found "significant support among small-business owners for increasing the minimum wage" (Jacobe 2006). In fact, 86 percent of those polled said the minimum wage did not have an impact on their business. Another five percent said the minimum wage had a positive impact.

Crying Wolf: Minimum Wages Ruin Economies and Lives?

Even the economists who still argue that minimum wage laws have negative effects generally assert that those impacts are small. Despite this, minimum wage opponents have often resorted to extremes in their effort to stop Congress or state legislatures from setting or raising wage rates. While campaigning for president, Ronald Reagan said "The minimum wage has caused more misery and unemployment than anything since the Great Depression." In 1996, the "Save Jobs for Houston" committee

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[5] Burkhauser and Finegan conclude that disemployment effects are not the reason to oppose the minimum wage. Rather, they question whether a minimum wage is the most efficient policy tool for addressing low-wage worker poverty, and suggest the Earned Income Tax Credit instead.

put out ads against a proposal to establish a citywide minimum wage in Houston. The ads said the ordinance would lead to:

> Cops and firefighters yanked off the streets. Higher taxes. Thousands of jobs lost. Soaring prices for such essentials as food and prescription drugs. The wholesale destruction of small businesses. Streets riddled with potholes. Swollen welfare rolls (Burtman 1997).

Almost a decade later, in 2004, business groups in Florida took out ads against a proposed state minimum wage increase. The state had already been hit by four hurricanes that fall and the commercial suggested the minimum wage would be a fifth hurricane. The commercial showed senior citizens in hospital beds begging for help. The ballot contained these words from opponents: “If this amendment passes it could cost tens of thousands of Floridians their jobs, health care coverage and retirement benefits. In addition, 18,000 children will lose their health care if this passes.”

Yet despite these terrifying statements, opponents have not been able to produce studies after the fact proving than the claims came true. Instead, the claims get repeated with each new campaign, and presented as fact that may be too complicated for non-economists to understand. In Oregon, Republican Gubernatorial candidate Chris Dudley remarked that Oregon’s high minimum wage has a negative impact on the state, but that he would not propose to change it because “it's a hot button that people don't really understand” (Mapes 2010). American Enterprise Institute scholar and former McCain presidential advisor Kevin Hassett said recently that the reason for high unemployment in the U.S. is that wages are too high, and that minimum wages should be lowered from $7.25 to $5.85 an hour. Hassett wrote in September 2010 that “Increasing labor costs via higher minimum wages at any time poses a risk of higher unemployment; doing so during a recessionary labor market is policy negligence,” and that policymakers are “ignoring the facts.” It appears that no matter what empirical studies say, minimum wage opponents will create their own facts.

Clearly, minimum wage opponents will continue to cry wolf. Policymakers and voters should not be distracted by the noise. It isn’t that the average person doesn’t understand economics; it is the average minimum wage opponent that refuses to examine the evidence.

Appendix A: Minimum Wage Studies and Resources

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Minimum Wage Studies and Resources

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<u>Resources</u>

Economic Policy Institute, www.epi.org

National Employment Law Project, www.nelp.org

Political Economy Research Institute, www.peri.umass.edu

University of California-Berkeley Labor Center, http://laborcenter.berkeley.edu/