



TESTIMONY

April 8, 2015

ON THE ENACTMENT OF A “LIVING WAGE” IN KANSAS CITY

By Michael Rathbone

Testimony Before the Planning, Zoning, and
Economic Development Committee

To the Honorable Members of the Committee

My name is Michael Rathbone, and I am a policy researcher for the Show-Me Institute, a nonprofit, nonpartisan Missouri-based think tank that supports free-market solutions for state and local policy. The ideas presented here are my own. This testimony is intended to summarize research regarding minimum-wage increases, in particular the potential effects of Ordinance #150217.

Minimum-wage laws are popular. In 2014, four states (Alaska, Nebraska, South Dakota, and Arkansas) voted to increase their states' minimum wage by large margins.¹ People in favor of raising the minimum wage argue that it will help poor and low-income families. For example, the late Senator Edward Kennedy argued, “The minimum wage was one of the first—and is still one of the best—anti-poverty programs we

have.”² Ordinance #150217 stresses the need for working persons to “earn wages that ensure a decent and healthy life.”³ It also states that “many who are employed do not earn sufficient wages to be self-sufficient.”⁴

Most people, me included, want higher wages for everybody. However, mandating a higher minimum wage as a way to improve the economic conditions of poor families is suspect.

Outline of the Proposed Ordinance

Ordinance #150217 contains the following provisions:⁵

- Effective September 1, 2015: The minimum wage will be increased to ten dollars (\$10) an hour.
- Beginning September 1, 2017: The minimum wage shall increase in increments of one dollar and twenty-five cents (\$1.25) a year for four years. By September 1,

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2020, the minimum wage will be fifteen dollars (\$15) an hour.

- Employees that earn more than thirty dollars (\$30) per month in tips/commissions shall be paid a base wage of six dollars (\$6) per hour—sixty percent (60%) of the minimum wage.
- Wage increases for tipped employees will occur simultaneously and proportionally to the increases in the minimum wage so that the base wage of the tipped employees remains 60 percent of the minimum wage.
- Tips and commissions are to be counted as part of employees' wages. If tips and commissions along with the base wage do not equal the minimum wage, the employer shall pay the employee the difference.

Economic Effects of Raising the Minimum Wage

One of the reasons that raising the minimum wage might not improve the conditions of poor families is that a higher minimum wage could discourage employers from using the low-wage, low-skilled employees that proponents of the minimum wage are trying to help. A large body of evidence confirms that minimum wages reduce employment for these workers.⁶ In one analysis of proposed federal minimum-wage increases, the Congressional Budget Office (CBO) estimated that an increase to the federal minimum wage to \$10.10 an hour would reduce employment by 500,000 jobs.⁷

In simple economic analysis, there are two main reasons why this occurs. The first is that employers will start using relatively less labor due to the increase in its cost. Instead, they will substitute other inputs, such as capital, that may now have a lower cost because of the increase in wages. This will lead to some employers reducing employment.⁸ The second is that since costs are higher due to higher wages, the prices of the products firms provide rises, reducing the demand for each firm's product and leading to a reduction in the scale of each firm's operation.⁹

This ordinance eventually would raise the minimum wage above the \$10.10 an hour examined in the CBO study.¹⁰ If raising the minimum wage to \$10.10 an hour is enough to cause significant job losses nationally, raising it to \$15 an hour potentially could have serious negative effects on employment in the area. This is especially true for Kansas City, since it shares a border with Kansas, which not only has a minimum wage of \$7.25 an hour, but also has many businesses that face income tax rates much lower than those in Missouri.¹¹ Kansas City businesses that rely heavily on low-skilled labor could find themselves at a competitive disadvantage compared to businesses on the other side of the border.

The second reason why raising the minimum wage is suspect is that it harms the earnings power of low-skilled workers. Dr. Jeffrey Clemens of the University of California, San Diego and Michael Wither, a graduate student at the University of California, San Diego, estimated the minimum wage's impact on

employment and income growth for low-skilled workers.¹² They found that increasing the minimum wage reduced the chances of low-skilled workers eventually reaching salaries of \$1,500 a month.¹³ Clemens and Wither believe that this reduction in mobility occurs because an increased minimum wage reduces the number of jobs available for poorer workers. Numerous studies, including the CBO, lend evidence to support that finding.¹⁴

Specifically, the authors state that:

It appears that binding minimum wage increases blunted these workers' prospects for medium-run economic mobility by reducing their short-run access to opportunities for accumulating experience and developing skills. This period's minimum wage increases may thus have made the first rung on the earnings ladder more difficult for low-skilled workers to reach.¹⁵

This observation makes sense given that minimum-wage workers are on the steep portion of the wage-experience profile (i.e., small gains in experience correspond to increases in wages), and a lack of employment will hold back these workers' wage growth.¹⁶ In fact, according to one study, the average minimum-wage worker will experience a 20 percent increase in wages if employed at the same job after a full year.¹⁷ Again, in this instance, increasing the minimum wage actually hurts those people proponents aim to help.

Finally, increasing the minimum wage is not a very effective means of helping low-income families. David Neumark, in his 2012 policy study for the Show-Me Institute examining the economic effects of the minimum wage, found that “there is no basis for concluding that minimum wages reduce the proportion of families living in poverty or near poverty.”¹⁸ The reason why the minimum wage is not especially helpful at lifting people out of poverty is because it benefits **low-income workers**, not **low-income families**. According to Dr. Neumark’s calculations, only 12.7 percent of workers making minimum wage or less are at or below the poverty line. In fact, nearly half (44.6 percent) of workers making at or less than the minimum wage were in households with incomes three times the poverty line or higher.¹⁹

This is the reason why even proponents of the minimum wage argue that it is a “blunt instrument” for helping low-income families.²⁰ Christina Romer, President Obama’s former head of the Council of Economic Advisors, agrees that increasing the minimum wage is not a very well targeted anti-poverty proposal.²¹

Summary

Raising the minimum wage sounds like good policy. As evidenced by its continued support at the ballot box, many people find mandating raises for low-income workers appealing. However, from an economic perspective, increasing the minimum wage can hurt those whom it seeks to

help while having little to no effect at helping poor families. People from across the ideological spectrum believe there are more effective means to helping the working poor than increasing the minimum wage.²²

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NOTES

1 Josh Barro, “Four States Vote to Raise the Minimum Wage,” *The Upshot*, November 3, 2014, <http://www.nytimes.com/2014/11/05/upshot/election-results-2014-minimum-wage.html?ref=2014-midterm-elections&abt=0002&cabg=1>.

2 Quoted in Andrew Clymer, *Edward M. Kennedy: A Biography* (New York: William Morrow & Co. 1999), 449.

3 Jermaine Reed, “Ordinance #150217,” Kansas City City Council, March 26, 2015, <http://cityclerk.kcmo.org/liveweb/Documents/Document>.

4 Ibid.

5 Ibid.

6 David Neumark and William Wascher, “Minimum Wages and Employment,” *Foundations and Trends in Microeconomics* 3, nos. 1-2 (2007): 1-186, http://www.socsci.uci.edu/~dneumark/min_wage_review.pdf.

7 Congressional Budget Office, “The Effects of a Minimum-Wage Increase on Employment and Family Income,” Congressional Budget Office Report, February 2014, <http://www.cbo.gov/sites/default/files/cbofiles/attachments/44995-MinimumWage.pdf>.

8 In the real world, laborers have different skill levels. Instead of reducing total employment, employers might substitute low-skilled workers for higher-skilled workers in response to a minimum wage

increase. This is important as any measure over overall effects on overall employment due to a minimum wage increase might be quite small. However, the negative employment effects on low-skilled, low-wage workers the minimum wage is intended to help can be quite large.

9 David Neumark, “Should Missouri Raise its Minimum Wage?” Policy Study, Show-Me Institute, 2012, <http://www.showmeinstitute.org/publications/policy-study/red-tape/821-should-missouri-raise-its-minimum-wage.html>.

10 Jermaine Reed, “Ordinance #150217,” Kansas City City Council, March 26, 2015, <http://cityclerk.kcmo.org/liveweb/Documents/Document>.

11 Kansas’ Minimum Wage: K.S.A. 44-1203, http://kslegislature.org/li/2014/b2013_14/statute/044_000_0000_chapter/044_012_0000_article/044_012_0003_section/044_012_0003_k/; Kansas’

state income tax rate: K.S.A. 79-32,110, http://kslegislature.org/li/b2015_16/statute/079_000_0000_chapter/079_032_0000_article/079_032_0110_section/079_032_0110_k/; Missouri income tax rate: RSMo. 143.011, <http://www.moga.mo.gov/mostatutes/stathtml/14300000111.html>; Kansas City Earnings Tax: RSMo. 92.120.1, <http://www.moga.mo.gov/mostatutes/stathtml/09200001201.html>.

12 Jeffrey Clemens and Michael Wither, “The Minimum Wage and the Great Recession: Evidence on Effects on the Employment and Income Trajectories of Low-Skilled Workers,” *NBER Working Paper 20724*, November 24, 2014, <http://econweb.ucsd.edu/~mwither/pdfs/Effects%20of%20Min%20Wage%20on%20Wages%20Employment%20and%20Earnings.pdf>.

13 The authors determined that \$1,500 a month was the threshold for lower-middle-class salaries.

14 David Neumark and William Wascher, "Minimum Wages and Employment," *Foundations and Trends in Microeconomics* 3, nos. 1-2 (2007): 1-186, http://www.socsci.uci.edu/~dneumark/min_wage_review.pdf; Congressional Budget Office, "The Effects of a Minimum-Wage Increase on Employment and Family Income," Congressional Budget Office Report, February 2014, <http://www.cbo.gov/sites/default/files/cbofiles/attachments/44995-MinimumWage.pdf>.

15 Jeffrey Clemens and Michael Wither, "The Minimum Wage and the Great Recession: Evidence on Effects on the Employment and Income Trajectories of Low-Skilled Workers," *NBER Working Paper 20724*, November 24, 2014, <http://econweb.ucsd.edu/~mwither/pdfs/Effects%20of%20Min%20Wage%20on%20Wages%20Employment%20and%20Earnings.pdf>.

16 Clemens and Wither cite: K.M. Murphy and F. Welch, "Empirical-age Earnings Profiles," *Journal of Labor Economics*, 1990, 202-229, <http://people.terry.uga.edu/mustard/courses/e8420/Murphy-Welch-Age.pdf>. This report also supports the fact that many minimum-wage workers are in a position where wage increases are most pronounced. See: U.S. Bureau of Labor Statistics, "Characteristics of Minimum Wage Workers, 2013," BLS Reports Report 1048, March 2014, <http://www.bls.gov/cps/minwage2013.pdf>.

17 R.E. Smith and B. Vavrichek, "The Wage Mobility of Minimum-Wage Workers," *Industrial and Labor Relations Review*, 82-88, <http://kumlai.free.fr/RESEARCH/>

[THESE/TEXTE/MOBILITY/mobility%20salariale/Wage%20mobility%20of%20minimum%20wage.pdf](#).

18 Neumark, "Should Missouri Raise Its Minimum Wage?"

19 Ibid.

20 David Card and Alan B. Kruger, *Myth and Measurement: The New Economics of the Minimum Wage* (Princeton: Princeton University Press. 1995).

21 Christina D. Romer, "The Business of the Minimum Wage," *New York Times*, March 2, 2013, http://www.nytimes.com/2013/03/03/business/the-minimum-wage-employment-and-income-distribution.html?_r=0.

22 The Neumark policy study (2012), the Clemens and Wither paper, the CBO report, and Romer all agree that increasing the Earned Income Tax Credit (EITC) is a more effective means at helping poor families. Whether doing so is a practical option for this jurisdiction is up for the jurisdiction to determine.



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