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An Analysis of the Minimum Wage and a Proposal for Future Policy Initiatives

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AN ANALYSIS OF THE MINIMUM WAGE
AND A PROPOSAL
FOR FUTURE POLICY INITIATIVES

BY

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PREFACE

Thirty three million Americans, 14 percent of the entire population, are estimated to be living in poverty. A popular conception of such people is that they either cannot or will not work. While it is true that a sizeable portion of those in poverty cannot work because of their age or their health, and there are undoubtedly some people who prefer poverty to work, a very substantial portion of those living in poverty, approximately 9.1 million, are members of families where at least one member works, and often works full-time (Smith and Varichek 1987).

There has been an ongoing controversy for at least the last thirty years over the direction that government policy should proceed as concerns poverty. Few federal policy questions have attracted so much basic disagreement. Numerous books, studies, and papers have been published that all offer prescriptions for the reduction or total elimination of poverty. Most of those formulas either call for raising the minimum wage or abandoning it. Perhaps no other question so neatly categorizes authors into two opposing ideologies, liberalism and conservatism. The liberals see the minimum wage as positive policy, a powerful tool that can enable those on the bottom rung of the economic ladder to accrue the basic necessities for a humane standard of living. Michael Harrington, a widely respected author and political activist, states in his book, The New American Poverty, that "No one who works full-time should be poor . . . the minimum wage and the various support programs should be set at levels that guarantee a nonpoverty income for every working citizen of the United States." (Harrington 1984, 248).

On the other hand, Edward C. Banfield, a noted scholar and educator tells us, in The Unheavenly City Revisited, to " . . . remove impediments to the employment of the unskilled, . . . by repealing the minimum wage. . . ." (Banfield 1974, 269). The conservatives view the minimum wage as contributing to increased unemployment - a negative policy. They explain that it reduces the number of jobs that are available due to the artificially high cost of labor.

These opposing opinions are not just restricted to the ranks of scholars and theorists but take on very real meaning in a forum that can have profound effect on every low income family in America, the United States Congress. The following viewpoints were expressed in testimony before the Senate Committee on Labor and Human Resources during minimum wage hearings in July of 1987. Lane Kirkland, president of the AFL-CIO stated the liberal position:

> A fair minimum wage is a policy issue and most fundamentally an issue of self-worth for individuals and self-respect for a nation that doesn't want to exploit anyone for the benefit of others. America must not allow the economic exploitation of its weakest workers - it must maintain a fair minimum wage (Congressional Digest 1987, 66:208).

Mr. Walter Ellis, Jr., president of the American Farm Bureau Federation, ably expressed the conservative fear:

> Numerous studies have shown that the federal minimum wage does not accomplish its original purpose of alleviating poverty. Any increase in the minimum wage will reduce available jobs . . . this bill could destroy a half-million jobs (Congressional Digest 1987, 66:203).

Curiously, both liberals and conservatives cite economic theory and both produce seemingly endless streams of data to prove their point; more curiously, both sides present convincing arguments. The liberals say a strong minimum wage is good for society; the conservatives tell us it is bad. The purpose of this paper is not to solve this dilemma, but to examine its basis and to more fully understand the conflicting viewpoints.

This is a paper about the minimum wage and how it affects a substantial number of Americans living in poverty. It concerns those workers who, for whatever reason, are at the bottom of the wage scale pyramid and for whom even full-time employment is insufficient to raise themselves and their families out of poverty. It is also about the minimum wage as an incentive for those in poverty to choose gainful employment as an alternative to relying on federally sponsored welfare programs.

Chapter one will explain the origins and development of minimum wage legislation as well as provide a thorough examination of the current law and its coverage. The second chapter will present the classical arguments of orthodox wage theory and examine the important concepts of labor supply, demand, and elasticity. It will also address the popular neo-classical economic theories, internal and dual labor markets, which are probably closer to the way the economy really works. Some current labor demand elasticity estimates will be presented to show the derived effects upon jobs and incomes if the estimates and theories are accurate.

In chapter three the role of the minimum wage as it pertains to poverty and the working poor will be covered as well as its potential costs and benefits to society. Regardless of the economic theory and statistical measurements one chooses to subscribe to, the bottom line in federal wage policy is political. Chapter four will examine the issues and goals of such policy in the political context and provide a description of the political arena in which the legislation must compete.

Any recommendation for change should be one that can realistically be expected to attain the maximum societal benefit at the minimum societal cost. It must also be one that is palatable to both liberals and conservatives as well as one that can compete well amongst the other agenda priorities of a shrinking federal budget. Chapter five will attempt to present just such a recommendation.

CHAPTER ONE

BACKGROUND

History

Proposals for government regulation of hours and wages first arose in this country in the late 19th century. The widely accepted philosophy of the period, at least the philosophy of those in economic positions from which they could be heard, was Social Darwinism. The philosophy placed great emphasis on individualism and self-reliance and interpreted economic success or failure as natural and just conditions. "Survival of the fittest" justified protecting employer interests with no regard for the rights of the employed. Mandating employee protections such as wages and hours represented a conflict between laissez-faire economic ideals and society's altruistic concern for the welfare of its deprived citizens (Levitan, Carlson, and Shapiro 1986). That conflict persists today.

In 1892 Congress first established standards for employee protection within the federal government. It was not an attempt to regulate private industry but merely an avowal by an individual employer, the government, to provide wage and hour guidelines for its own employees. This was the origin of the eight-hour day.

Early attempts to regulate the private sector in this regard were undertaken by individual states, not the federal government. In 1912 Massachusetts enacted the first minimum wage law and this precedent was quickly followed by eight more states the following year. State laws generally provided for industry wage boards to establish the standards rather than mandating state-wide requirements. Furthermore, most of the early laws covered only women and minors and were not vigorously enforced. As the movement toward state regulation spread it was continually challenged in the courts. By 1930, although seventeen states had previously enacted minimum wage laws, seven were found to be unconstitutional and three had been repealed. The remaining seven states enforced their laws with great trepidation (Levitan and Belous 1979).

Renewed interest in employee protection grew out of the economic hardship wrought by the Great Depression. In 1933 Congress passed the National Industrial Recovery Act which was the first federal move into labor regulation in the private sector. It recognized labor as an economic entity and attempted to reverse the problems of the depression through a new cooperation between government, business, and labor. Although ruled unconstitutional by the U.S. Supreme Court in 1935, the National Industrial Recovery Act had established labor's identity as a party to the depression crisis (Levitan and Belous 1979).

In 1937 President Franklin D. Rossevelt requested legislation to establish federal wage and hour standards. The standards were to apply to all workers and, patterned after earlier state laws, were to be administered by a wage and hour board on an industry by industry basis. President Roosevelt's much amended proposal became law in 1938 as the Fair Labor Standards Act (FLSA).

The FLSA specified a minimum wage and established the 40-hour work week. It also required payment of an overtime premium and restricted child labor. The purpose of the law was to require employers to pay a socially acceptable return on labor and to spread employment opportunity by requiring overtime pay for hours worked in excess of the standard work week (CCH 1985). The original act set the wage floor at 25 cents an hour with stepped increases to 40 cents an hour by 1945. FLSA coverage, however, was narrowly defined as pertaining to those workers directly engaged in interstate commerce or in the production of goods for interstate commerce. Thus restricted, and with numerous exemptions, the Act only covered 25 percent of the workforce. It excluded large segments that were most in need of the protection such as retail trade, service, and agriculture (Levitan, Carlson, and Shapiro 1986).

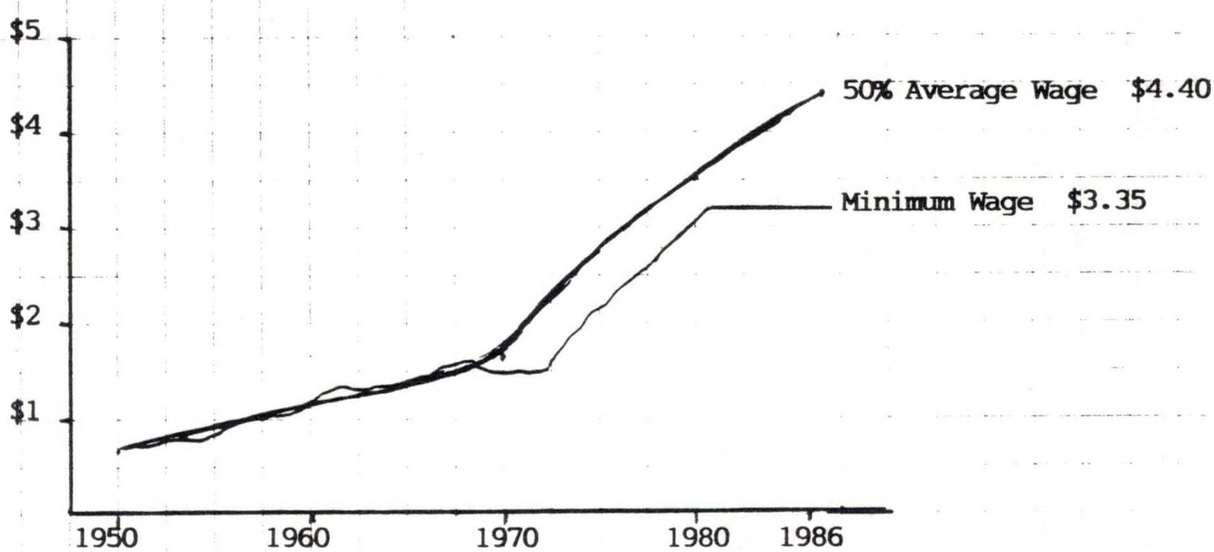
Congress has since amended the act on several occasions resulting in both increases in the wage rate and in expansion of coverage. In 1949 the wage floor was increased to 75 cents an hour and then to one dollar in 1955; to $1.25 in 1961, and to $1.60 effective in 1968. The 1977 amendment increased the minimum wage in stair-step fashion to $2.65 effective in 1978, $2.90 for 1979, $3.10 for 1980, and to $3.35 to be paid in 1981. Each increase was accompanied by lengthy debate and by reevaluation of the entire minimum wage concept.

In the 1949 amendment there was a general readjustment of industries covered, while some previous exemptions were removed, many were added. The amendment effectively decreased the coverage of the FLSA primarily for employers of small numbers of workers. In 1958 numerous bills expanding coverage were debated but it was not until 1961 that coverage was appreciably increased. The 1961 law provided for interim sub-minimum wages that could be paid by newly covered employers which increased to the national minimum by 1965. Coverage was again expanded in 1966 and, again, an interim sub-minimum was allowed until 1971 to ease the burden on the newly covered employers. For the first time workers in agriculture came under minimum wage protection, albeit at reduced rates and with numerous stipulations. The 1966 amendment was important also in that it covered workers in many areas of public employment such as schools, mass transit, and state-run institutions. Congress continued its expansion of coverage in 1974 and again in 1977 to the point where today nearly ninety percent of the total nonsupervisory workforce is subject to the law (Congressional Digest 1987,66).

The minimum wage has been traditionally set at roughly fifty percent of the average hourly wage paid to nonsupervisory workers in private industry (Cohadas 1987). It should be noted that during the 1950's and 1960's there was a close relationship between them with a slight, but not expansive, departure from tradition during the 1970's (see Table 1).

TABLE 1

MINIMUM WAGE vs. 50% AVERAGE WAGE



Source: Congressional Quarterly Weekly Report, 45, March 7, 1987, p.404

ıce 1981, while average wages have continued to climb, the minimum ɟe has been frozen at $3.35. For the past eight years the ratio of :nings allotted to the minimum wage earner has shown relative decline the point where in 1987 it constituted only about thirty eight percent the average nonsupervisory wage. To readjust the 1987 wage floor traditional standards would have required an increase of about $1.05 hour to $4.40.

rrent Coverage

While approximately ninety percent of nonsupervisory hourly paid rkers are now subject to the provisions of the FLSA, ten percent, approximately eight million, receive no minimum wage protection ;mith and Vavrichek 1987). An examination of the coverage is now in ·der.

<u>›vered</u>

As originally enacted the FLSA applied only to those workers directly ıgaged in interstate commerce. Since 1938 the volume of interstate ɔmmerce has expanded dramatically as well as the number of employers hus engaged. The various amendments to the act have also expanded he meaning of interstate commerce to include many other types of jobs. lanufacturers who produce goods that will cross state lines, those engaged .n interstate communications, and wholesalers whose employees receive, ›rder, or keep records of goods between states are all subject to the law. It also covers employees who mine, produce, process, or distribute goods even though those goods may eventually leave the state through another company. Furthermore, the law applies to all employees of a covered employer regardless of an employee's specific duties. Thus, a janitor for such a company is also covered even though his or her job is not directly related to interstate commerce.

In addition to those employees loosely construed as being engaged in interstate commerce, the law now applies specifically to laundries and dry cleaners, construction, health care, higher education, retail and service businesses with yearly sales of $365,000 or more, and to any other employer with annual sales or income of at least $250,000. It also covers such casual workers as maids, day workers, housekeepers, chauffers, cooks, and full-time babysitters if they receive at least fifty dollars in wages in any calendar quarter (Hunt 1984).

Uncovered

Employees not covered include those who work for independent retail and service businesses with annual sales of less than $365,000 and other employers who do not meet the interstate commerce criteria and also have incomes of less than $250,000 a year. Exemptions from the Act are also specifically provided for executive, administrative or professional employees, outside sales persons, or employees of amusement or recreational businesses having seasonal peaks. Although most agricultural and fishing industry employees are subject to minimum wage provisions, they are not afforded overtime protection. Part-time babysitters and companions for old or ill people who cannot care for themselves are totally uncovered as are, of course, those that are self-employed (CCH 1985).

One modification to the minimum wage pertains to employees who work in jobs where they customarily receive tips, such as food servers and some hotel employees. The law stipulates that if workers receive over $30 a month in tips then the employer is allowed to take a tip credit of up to 40 percent of the hourly minimum. Thus, tipped employees may be paid as little as $2.01 per hour with the remainder of the minimum being derived through the tips they receive. (CCH 1985). Employers must be continually aware of the amount of tips received to know that individual employees are receiving the minimum. Conversely, employees should be knowledgeable of the law to be sure that they are receiving what they should. There is little evidence to indicate that either is the case (Levitan, Carlson, and Shapiro 1986).

A further provision of the law permits full-time students to be employed at 85 percent of the federal minimum, or $2.85 an hour. Such employment may be part-time during the school year or full-time during vacation periods. Employers in retail or service businesses, agriculture, or higher education may take advantage of this provision through a certification procedure from the Department of Labor. Employers of handicapped persons in sheltered workshops and learners in industries other than retail or service may also receive certification to pay subminimum wage rates (Congressional Digest 1985,64). Although the rules and stipulations governing subminimum employment are complicated, most requests are approved pro forma (Levitan and Belous 1979).

The separate states and jurisdictions are free to establish their own minimum wages above that of the federal law or to extend coverage to the uncovered areas. All but nine states, primarily in the south, have legislated one or the other, or both, forms of wage action. Coverage is currently provided for all employees in eighteen jurisdictions. Ten of those; Alaska, Connecticut, the District of Columbia, Hawaii, Maine, Massachusetts, Minnesota, New Hampshire, Rhode Island, and Vermont, have established universal coverage that is higher than the federal minimum. Although the provisions of the FLSA have remained unchanged since 1981, that has not been the case among the states. In 1987 alone seventeen states took action to increase their rates and/or extend their coverage (CCH 1985) (Nelson 1988).

The responsibility for enforcing the minimum wage rests with the Wage and Hour Division of the Labor Department. Employers can be fined for violations as well as be required to make restitution in the form of back-pay to individual employees. Court action may be sought by individual employees, groups of employees, or by the government on behalf of employees. Suits may not, however, be brought by unions (CCH 1985). The majority of the Division's investigatory effort is spent in evaluating employee complaints and allegations. When a violation is found to have occurred the employer is normally given the opportunity to comply voluntarily before being taken to court. This process assumes that most employees are aware of the minimum wage laws and that they are willing to file complaints. Some workers, even if they are aware of the laws, may be afraid to file complaints against their employers for fear of losing their jobs. Naturally illegal aliens, undercutting the wage protection afforded American workers to the advantage of unscrupulous employers, would not be inclined to file complaints. Attempts to specify the extent to which violations currently occur would be tenuous at best. Suffice it to say that at least some employees who are covered under the law are not receiving the minimum wage (Levitan and Belous 1979).

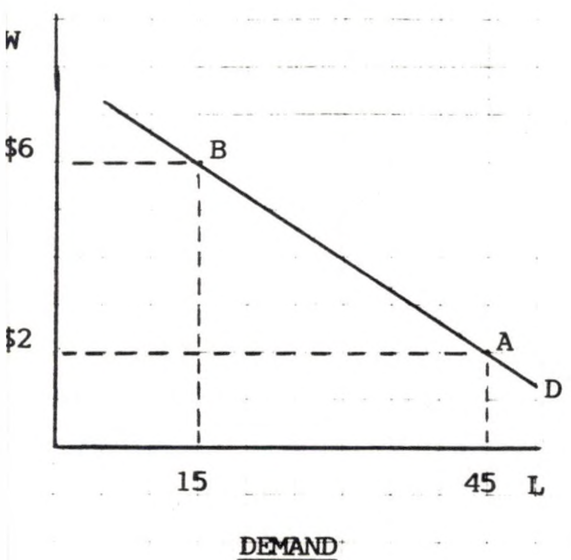
CHAPTER TWO

ORTHODOX WAGE THEORY

Supply, Demand, and Elasticity

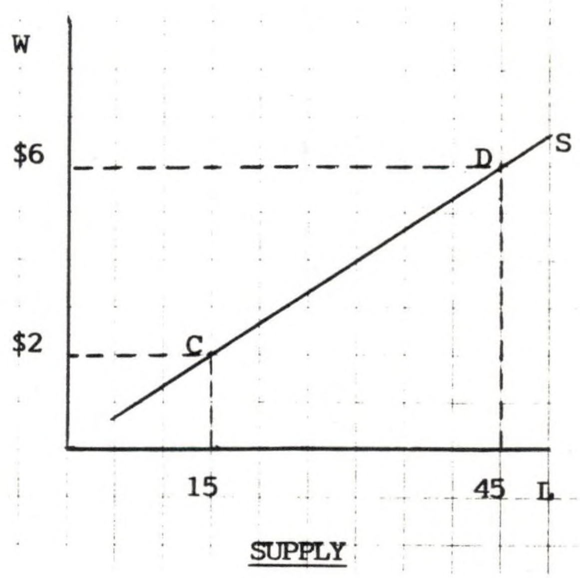
The basic disagreement between liberals and conservatives as to the desirability of the minimum wage can be illustrated through rudimentary orthodox wage theory. In figure 1 the vertical axis represents wages per hour and the horizontal axis numbers of employees. The diagonal curve, D, represents the labor demand of a theoretical employer. In this simplistic representation it is shown that forty five employees will be hired when the wage rate is $2.00 per hour, point A on the demand curve. If the cost of labor, wages, increases to $6.00 per hour the employer will only wish to hire fifteen employees, point B. The demand curve is downward sloping because the employer wishes to add employees only to the point where the added cost of each equals the added contribution of their productivity. This reflects a basic economic principle that the price (wages) should equal the value of the marginal product of each unit of production (labor).

FIGURE 1



DEMAND

FIGURE 2

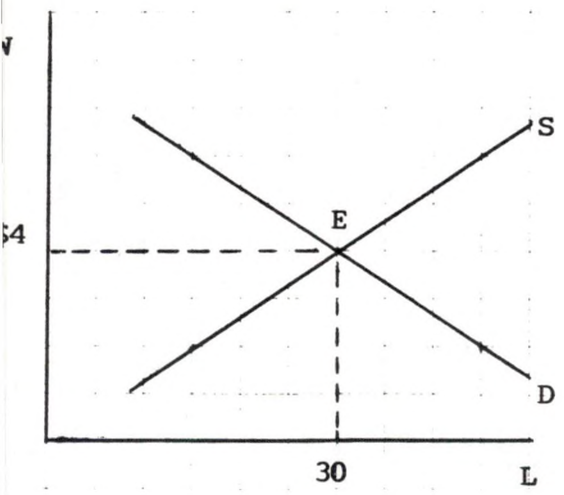


SUPPLY

However, the demand for labor is only part of the picture, supply must also be considered. Figure 2 represents the same wage and labor quantity relationship but this time labor supply, the number of persons willing to be hired, is shown by the diagonal curve, S. Suppose the theoretical employer is paying wages of $2.00 per hour, there may be fifteen people willing to work, point C. If, for some reason, the employer raises the hourly wage to $6.00, there will now be forty five people willing to be employed, point D. The supply curve is upward sloping because raising the hourly wage induces more people to view that wage as preferable to the returns of not working.

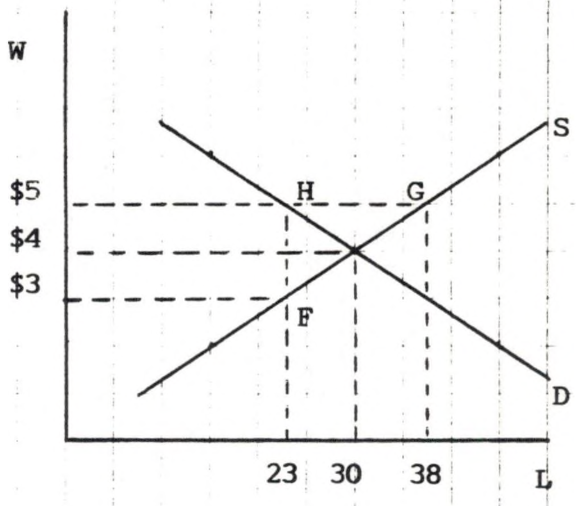
If the demand and supply curves are superimposed, as in figure 3, the combined effects are shown. A given hourly wage will induce a certain number of people to want to work, but the employer will only pay a wage up to the marginal productivity of each additional worker. In this case the model indicates equilibrium at point E, thirty workers earning $4.00 per hour each. Should the employer pay less than $4.00, he would restrict the number of employees willing to work and therefore his profits. If he paid more than $4.00, he would be able to hire more workers but their productivity would be less than what he is paying them and the employer would lose money. Conversely, thirty people will be willing to work at $4.00. Those requiring something less than $4.00 an hour for their time would be happy to accept the increased benefits. Those who value their free time more than $4.00 an hour would choose not to work. The forces of supply and demand, then, create a natural equilibrium in the wage rate and labor quantity relationship, point E, allowing both the employer and the employees to obtain the maximum benefit in light of the constraints produced by the other (Hamermesh 1984).

FIGURE 3



EQUILIBRIUM

FIGURE 4



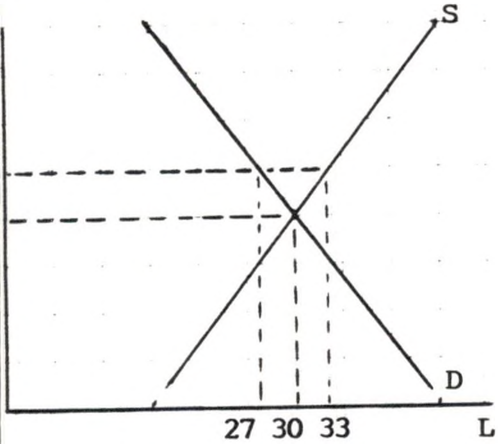
JOB LOSS

Now consider the minimum wage which artificially changes the relationship, see figure 4. If a minimum wage is established below the equilibrium point, say at $3.00, point F, there will be no change in the relationship. The employer will still offer $4.00 and he will still find thirty willing employees. However, should the wage floor be arbitrarily set at $5.00 an hour, while as many as thirty eight people will be willing to work for the higher wage, point G, the employer will only be willing to hire twenty three, point H. To hire more than twenty three people at the higher wage rate would entail paying more than the value of the marginal productivity of the additional workers. Thus, if the cost of labor is raised to $5.00 an hour, seven people will lose their jobs and become unemployed. This is not the only effect of forcing up the wage rate. Whereas at $4.00, thirty people were willing to work, at the new rate of $5.00 thirty eight people are seeking jobs. Rather than just adding the seven people who lost their jobs to the number of unemployed, the additional eight job seekers must be added for a total of fifteen.

This is because the level of unemployment is defined not just as job losers, but includes those who would be employed at the current wage rate if an opening were available (Levitan and Belous 1979).

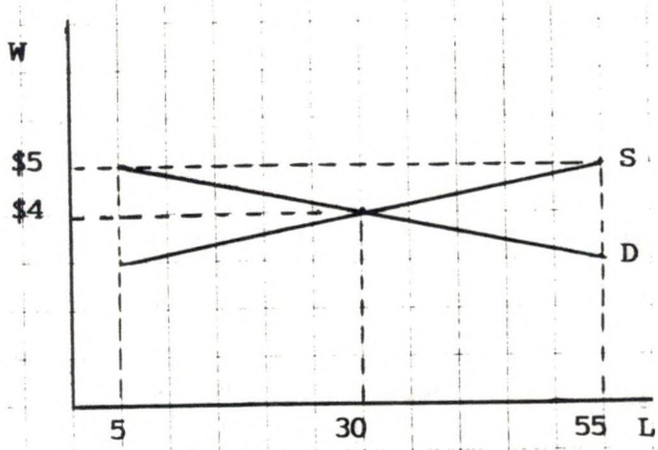
It is clear in this scenario that by establishing the minimum wage at $5.00, one dollar above the equilibrium wage, that fifteen people are now considered unemployed. But the relationship of one dollar to fifteen people is by no means constant, it depends upon the slope of the curves. Consider if the slopes of the curves are altered as in figures 5 and 6.

IGURE 5



LOW ELASTICITY

FIGURE 6



HIGH ELASTICITY

In figure 5 the increase of one dollar an hour above equilibrium will result in the loss of only three jobs and a total increase in unemployment of only six people. However, in figure 6, with the slopes drastically altered, the one dollar increase will result in twenty five lost jobs and twenty five more people now seeking employment, for a total of fifty added to the ranks of the unemployed. Herein lies the crux of the disagreement between the liberals and the conservatives; what are the correct slopes of the supply and demand curves? The liberals would have us believe that they are fairly steep, as in figure 5, resulting in only small changes in the number of unemployed. The conservatives see the curves as flatter, figure 6, where a small increase in the minimum wage produces a large increase in the number of unemployed. The slopes of the curves indicate elasticity.

The concept of elasticity concerns the degree of change on one axis of the model, labor quantity, brought about by an incremental change on the other axis, wage rates. In other words, if the wage rate changes by one percent, what percentage of change in labor quantity will be observed? If a one percent change in wages causes exactly a one percent change in labor quantity, then the elasticity of demand equals one. But if a one percent change in wages produces less than a corresponding one percent change in labor quantity, then the elasticity of demand is less than one, as in figure 5. If it produces greater than a one percent change then the elasticity is greater than one, figure 6.

There is definitely a tradeoff between wage rates and the quantity of labor both demanded by, and available to, employers. There is no question that an artificially imposed minimum wage which is above the equilibrium wage will result in increased unemployment. To determine how much unemployment one needs to know the slopes of the curves, or, as represented as percentages of change, the elasticities (Hamermesh 1984). Since good elasticity estimates are vital to the determination, numerous studies have been conducted on this subject. Elasticity of labor demand not only varies greatly from industry to industry, but within industries as well. It is also constantly shifting due to technological change in production methods and changes in the price elasticities of product consumers. For instance, an industry whose costs of production can readily be passed on to consumers in the form of higher product prices, like a public utility, would have a labor demand elasticity of well under one. That is, as the cost of labor increases, very few workers would be laid off, the additional labor costs would simply be added to the product price. In very competitive industries, such as fast food enterprises, an increase in wages could not be readily passed on to the consumer. If they raised the price of their final product their customers would simply buy their fast food elsewhere. Although an increase in the minimum wage would theoretically raise all fast food prices simultaneously, the cost of labor is not the only factor involved. The increased costs may be met by some businesses through substitution of more efficient equipment for labor. Others may temporarily sacrifice profits to obtain a larger share of the market. Those businesses that are already operating at peak efficiency and with narrow profit margins would be forced to raise their hamburger prices and may lose many of their customers, perhaps even be forced out of business. Substitution of equipment for labor and business failures would both result in increased unemployment. In this case the elasticity of labor demand would be greater than one.

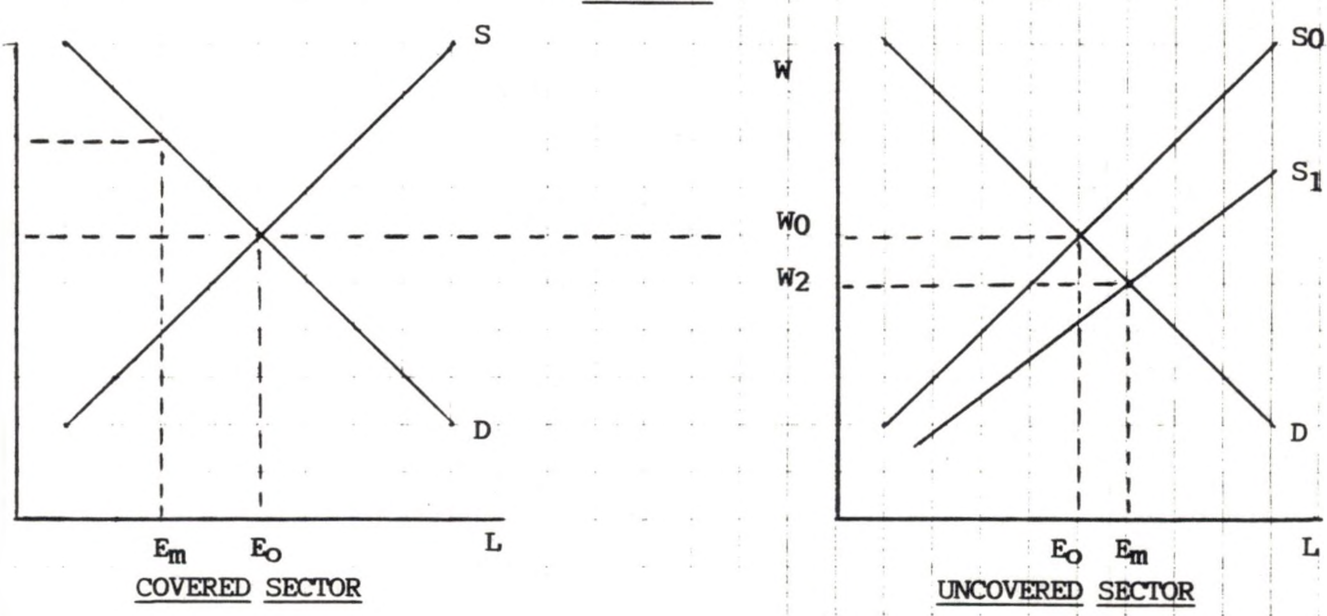
Another very important variable in the determination of labor demand elasticity is the impact of labor costs on the total price of the employer's product or service. If labor costs constitute a large proportion of product price then increases in wages would necessitate relatively large increases in product price or worker lay-offs. Conversely, where labor costs contribute to only a small proportion of the product or service price, then an increase in wages would produce only a small increase in price, an increase easily accepted by consumers resulting in few, if any, lay-offs. There are numerous other variables that also affect elasticity in this manner (Levitan and Belous 1979).

Since labor demand elasticities are so variable and because they are constantly changing, the numerous inquiries into the subject have produced a wide variety of answers. The liberals or conservatives have had only to select those studies which have shown elasticities that support their point of view.

Job Rationing

Figure 7 shows two supply and demand scenarios, the one on the left for the sector covered by the minimum wage provisions of the FLSA and the one on the right depicts employment not subject to the law, the uncovered sector. If there were no minimum wage, or if it were set at less than the equilibrium wage, then both sectors would remain at equilibrium; wages at W_0 and employment at E_0. When the minimum wage is introduced, above equilibrium, the covered sector is forced to raise wages to W_1 and employment is reduced to E_m. The non-covered sector

FIGURE 7



does not have to raise wages, but nor does it have to remain at the current equilibrium point. Because many of the workers who lost jobs in the covered sector must now look for employment in the uncovered sector, the supply curve in the uncovered sector shifts out to the right, S_0 to S_1, reflecting the spillover in job seekers. The uncovered sector can now seek a new equilibrium with wages at W_2 and employment at E_m. In this case, the minimum wage has resulted in higher wages for those still employed in the covered sector, but for those in the uncovered sector it has meant not only a decrease in wages, but an increase in the number of low paying jobs. The number of jobs lost in one sector and gained in the other will of course depend upon the elasticities involved. There will also be some workers who lose jobs in the covered sector who refuse to work at the low wages in the uncovered sector. They will either go on unemployment and continue to look for a job at the higher wage or may lose hope and drop out of the work force entirely.

The size of the labor supply shift in the uncovered sector caused by the spillover is very important. If the number of workers in the covered sector were small relative to the uncovered sector, the magnitude of the shift in the supply curve, for a given elasticity, would also be small. However, today's FLSA coverage applies to approximately ninety percent of the non-supervisory work force. If jobs were lost in the covered sector due to a mandated wage increase, the number of workers seeking jobs in the uncovered sector might increase dramatically. This would cause a pronounced shift in the uncovered supply curve and drive the uncovered wages even lower and the number of unemployed even higher. To rehire the total number of job losers in the uncovered sector would drive the wage rate to an unacceptably low level, a level so low that society would not be likely to accept it (Levitan and Belous 1979).

Neo-Classical Theories of Wages and Employment

While orthodox wage theory provides us with a workable model of the relationship between wages and employment, the operation of real world employment economics is probably more accurately described by a combination of two neo-classical theories; internal and dual labor markets.

Internal Labor Market

If an individual employee is engaged in piece work in a mass production setting it may be possible to accurately determine the value of his or her productivity. However, the value of most workers' productivity cannot be readily ascertained. It would be extremely difficult to measure the productivity of, for example, a secretary or a mid-level manager. Since specific valuations of productivity cannot be accurately determined for most jobs the pricing and allocation of labor is primarily assigned by a set of prescribed rules rather than by pure labor market forces. Thus, wages tend to be tied to specific jobs rather than to individual workers and workers receive pay increases primarily by working their way up the job scale through a series of promotions and seniority based on longevity with the employer.

This theory claims that most positions other than at the low paying entry level are filled through internal promotion. It also points out that most employers provide firm-specific training, that is, training of value in that specific firm but of relatively little value to the worker in seeking employment elsewhere. Because of this, lower level workers can normally be paid at a rate that is somewhat below the value of their production. On the other hand, as an incentive for remaining with the firm, mid and upper level employees are normally paid at a rate which is proportionately higher than their individual productivity. Thus the average wage may equal the average worker's productivity, but not that of the individual worker. Furthermore, there exists a certain wage rigidity in employment that prevents wages from decreasing in the short term in response to market conditions. Workers having become accustomed to a certain wage level will vigorously resist any decrease in that wage so long as they have any alternative.

The implications of the internal labor market are that most jobs other than at the entry level are filled from within, that firm-specific training ties lower level workers to the employer while they earn less than their value to the employer, and that upper level workers are paid somewhat more than their direct contribution to production. The extra pay earned by upper level workers is partially offset by their efforts in training those at lower levels and in providing the incentive for those at lower levels to do well at their jobs. This theory helps to explain why most companies have mandatory retirement guidelines for senior employees which put a cap on the wage scale. The concept of wage rigidity explains why most employers respond to market down-turns by laying off workers rather than by decreasing wages. To maintain the incentive that seniority provides, most lay-offs occur among the lower paid workers rather than their more senior and higher paid counterparts. Because once hired, an employee will eventually gain seniority and will become relatively expensive, applicants at the entry level are carefully screened. This makes it very difficult for the unemployed worker with few skills to be hired (Hamermesh 1984).

Dual Labor Market

The dual labor market consists of two separate and distinct markets, the primary and the secondary segments, with institutionalized barriers between them. The primary segment has the characteristics of the internal market just discussed. Workers are relatively well paid and have generally good working conditions. Job training and employment stability are the norm. Employees tend to be responsible and develop loyalties to the employer because they know that by doing so they will advance in seniority and receive the benefits of continued promotion opportunity.

The secondary labor market is characterized by low wages, favoritism, rapid turnover, and high unemployment. Employers in this market may have short or unpredictable production schedules, such as in agriculture or unskilled construction. The production process typically requires little or no training and none is provided. Workers generally do not have the opportunity for advancement to higher level jobs and formal seniority programs are nonexistent. Few employees develop any sort of loyalty to their employer nor are they apt to develop responsible work habits because there are no rewards for doing so. The poor work habits typical of employees in this market are not discouraged by employers and, in fact, the unreliable nature of the employment tends to reinforce and perpetuate those habits which, combined with lack of training, make the workers unacceptable in the primary market. It is a dead-end job market that exists to fulfill the needs of certain types of employers and from which the unskilled employees have little chance of escaping (Hamermesh 1984). This is the market in which the majority of minimum wage earners participate. Unless these workers can somehow develop their skills without the assistance of their employer, and unless they can learn responsible work habits without employer related incentive to do so, they will very likely never earn appreciably more than the minimum wage (Mellor 1987).

The existence of the neo-classical theories tends to weaken the validity of the strictly numerical application of orthodox wage theory. Predicting changes in the wage and labor quantity relationship through solely the orthodox approach leaves us with many unanswered questions. This is illustrated in the example that follows.

Estimating Job Loss Effects

As stated earlier, to estimate the job loss effects of an increase in the minimum wage, one needs to know the elasticity of labor demand. One such figure was estimated by combining the results of fourteen studies performed in the mid 1970's. The resultant overall one-year elasticity of labor demand in the United States was estimated to be -0.32 (Hamermesh 1976). The Minimum Wage Restoration Act of 1987, sponsored by Senator Edward M. Kennedy, called for increasing the minimum wage to $3.85 in 1988 (Congressional Digest 1987,66). At that time there were approximately 5.06 million hourly paid workers earning the minimum wage or less (Mellor 1987). Using these figures, a 14.9 percent increase in the minimum wage with an elasticity of -0.32, applied to 5.06 million workers, it can be determined that Senator Kennedy's proposal would have cost approximately 241 thousand jobs (see Footnote 1). While the loss of that many jobs would certainly have worked a hardship on the job losers, the overall

Footnote 1:

5,060,000 minimum wage jobs
1% increase = -0.32% jobs
14.9% increase = -0.32 X 14.9 = -4.768% jobs
5,060,000 jobs X -.04768 = 241,261 lost jobs

societal impact would have been positive in that the extra hourly earnings of the job keepers, $2.4 million, would have far outweighed the loss to the job losers, $.8 million, by a net gain of $1.6 million (see Footnote 2).

The pertinent question now becomes; even in light of the overall net monetary gain to workers, can our society tolerate putting that many people out of work? Furthermore, the elasticity estimate used was for one year; how many of those job losers will be rehired at the higher wage in subsequent years? How many of the job losers will be supporting a family on their income? How many will be teenagers in relatively affluent families working only for pocket money? Nor does the orthodox scenario consider the impact of neo-classical theories of employment. Will the majority of job losers be those with little chance of being rehired, those in the secondary job market?

The bottom line of this discussion and the purpose of this exercise is to show that even though high sounding economic data are continually used either to justify or condemn the minimum wage, that the projections thus derived are moot. The real-world implications of raising the minimum wage are not all addressed by the application of orthodox theory. The predictions do not give us the clear answers that its practitioners would have us believe. While a basic understanding of orthodox theory is extremely helpful in evaluating the minimum wage, one should not place too much emphasis on the numerical results. Especially considering that proponents and opponents select the data that best fit their need,

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Footnote 2:

5,060,000	total jobs
241,261	lost jobs
4,818,739	jobs retained

4,818,739 X $.50 wage increase	=	$2,409,369.50
241.261 lost jobs X $3.35	=	808,224.35
		$1,601,145.15 net gain

the evaluation of the subject is not so scientific as they would have us believe. The decisions that must be made must be based on normative values.

CHAPTER THREE

THE ROLE OF THE MINIMUM WAGE & POVERTY

Poverty and the Working Poor

Thirty three million Americans living in poverty, that means that approximately one in every seven Americans is officially considered poor and in need of one or more of the income subsidy or payment in kind programs, commonly called welfare (Smith and Varichek 1987). But how do we measure poverty, how did we arrive at this figure? Poverty is a relative concept and means different things to different people. Various terms are commonly used to describe poverty such as poor, needy, deprived, low income, and decent standard of living. Banfield even goes so far as to distinguish among degrees of poverty; destitution, want, hardship, and relative deprivation. He stated that in 1974 no one met his conditions of destitution; "Lack of income sufficient to assure physical survival and to prevent suffering from hunger, exposure, or remedial preventable illness." He did allow that many were considered to be suffering from relative deprivation, "Lack of enough income, status, or whatever else may be valued to prevent one from feeling poor in comparison to others" (Banfield 1974, 129-130). The real measure of poverty lies somewhere in between the extremes presented by Banfield. As with any concept, poverty cannot be definitively measured with adjectives or descriptions, we must resort to the use of numbers.

Our current official definition of the "poverty line" is derived from the work of Mollie Orshansky in 1963. Her strategy was to calculate the cost of a minimal diet, one which met the basic nutritional needs but with no frills, and multiply it by three. She used the number three because a 1955 Department of Agriculture survey determined that the average family spent one third of its after-tax income on food. Although it has been difficult to find wide agreement on what constitutes a nutritional, no frills diet and the factor of three has often been questioned, her formula is still in use today (Harrington 1984). Political manipulation of this formula is even easier than the application of selected statistical data as covered in the previous chapter. Small adjustments to the cost of the basic diet can result in statistically moving thousands of people in or out of poverty. Nevertheless, this is the formula currently used in our determination and the cost of the diet is periodically adjusted by changes in the Consumer Price Index. The 1987 poverty threshold for a single person was $5,590, for two people $7,230, for the three person family $8,570, and $10,990 for a family of four.

An individual who works full-time at the current minimum wage of $3.35 would earn just under $7,000 per year. Although a person supporting only him or herself on that income would not be judged by these standards to be in poverty, workers with one or more dependents would. Full-time employment at the minimum wage, and without deducting any lost time due to sickness or vacations, would place a family of two at 96 percent of the poverty level and families of three and four with only one such wage earner at 81 and 63 percent respectively.

Federal relief cash assistance programs, such as Aid to Families with Dependent Children, programs for the permanently and totally disabled, and for the blind provide for direct payments of money to qualifying persons or households. Payment in kind programs provide a commodity or service rather than money, such as food stamps, public housing subsidies, and Medicaid. Because each program is administered separately, some at the state level and others federally, and even some by different state or federal agencies, there is no single qualification criterion to be met. Each program has its own unique eligibility requirements (Bullock, Anderson, and Brady 1983). None of the programs are based exclusively on family income as compared to the poverty line and it is therefore difficult to determine at what income level equivalent we as a nation wish to support the poor.

It would be instructive to propose an example assuming that we were able to determine an income level at which we would want to provide support, say at 90 percent of the poverty level. If we have a hypothetical population of 300 full-time minimum wage earners, equally distributed with 100 supporting one other person, 100 supporting two others, and 100 supporting a family of four, we can come to some conclusions concerning the results of welfare and those of the minimum wage. The two person family groups would require no additional assistance because they are already earning 96 percent of the poverty level and we have established our hypothetical support level at 90 percent. To bring the three and four person families up to 90 percent, however, would require that we subsidize them with $745 and $2,923, respectively. The 100 three member households would require an annual government payment of $74,500 and

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Footnote 3:

3 member poverty level = $8,570 X 90% =	$7,713		
income =	6,968		
subsidy required	745	X 100 =	$74,500
4 member poverty level = $10,990 X 90% =	$9,891		
income =	6,968		
subsidy required	2,923	X 100 =	$292,300

$74,500 + $292,300 = $366,800 total subsidy required the four member units would require $292,300 for a total of $366,800 (see Footnote 3). Suppose now that we raise the minimum wage by 10 percent to $3.69. We will also use the average labor demand elasticity estimate that we used in the example in chapter two, -0.32. In this case it would be logical to conclude that three out of the one hundred wage earners of each family size would lose their jobs and have no income, whereas the other ninety seven wage earners would receive pay increases. To replace the total income of the job losers in each category would cost; two member, $19,521; three member, $23,139; and four member, $29,673, for a total of $72,333 (see Footnote 4).

On the other hand, there are some savings to be made through reduced support levels required by the job keepers. In this example the three member families would now only require a total of $4,656 and the four member families only $215,922 for a total annual subsidy of $220,578. Thus by raising the minimum wage by 10 percent we have reduced the annual government subsidy requirement from $366,800 to $292,911 for a savings of $73,889 (see Footnote 5).

The economic reality in the United States is that the choice for many minimum wage earners is not work <u>or</u> poverty, but work <u>and</u> poverty. 9.1 million Americans live in families where at least one person works yet their income is still below the poverty line (Smith and Varichek 1987). The point of the preceding example is that there is a definite trade-off between the established minimum wage and the total cost of

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Footnote 4:

2 member: 90% poverty level = $6,507 X 3 = $19,521
3 member: 90% poverty level = $7,713 X 3 = $23,139
4 member: 90% poverty level = $9,891 X 3 = $29,673
income replacement costs $72,333

federal and state assistance programs that we variously refer to as welfare. A prudently established minimum wage can greatly reduce the costs of that welfare. There are still other benefits of the minimum wage and there are costs. Examples of each are covered in the next section.

Benefits and Costs of the Minimum Wage

We have established that the relative merits of minimum wage policy cannot be determined solely through the use of econometric models. Numerous judgements are required that go beyond the capability of statistical manipulation. This study does not attempt to answer those remaining questions but merely mentions some of the more common issues which have been raised. It is left to the reader to evaluate the benefits and costs as presented here in accordance with his or her own values.

Benefits

The most obvious benefit of the minimum wage is that it raises the earning power of those at the bottom of the economic ladder. It can enhance the quality of life for millions of working Americans. If set high enough, it can raise many of them out of poverty and reduce the cost of current welfare programs to the taxpayer. It can increase the incentive for other welfare recipients to seek employment by increasing the returns of work relative to those of public assistance (Levitan 1979).

Footnote 5:

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3 member: 90% poverty level = $7,713
                     income =  7,665
         subsidy required     $   48 X 97 = $4,656

4 member: 90% poverty level = $9,891
                     income =  7,665
         subsidy required     $2,226 X 97 = $215,922
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\$4,656 + \$215,922 subsidy + \$72,333 income replacement = \$292,911
\$366,800 - \$292,911 = \$73,889 savings

Some proponents point out that ethnic minorities and women are disproportionately represented among minimum wage earners. They see the minimum wage as providing a mild form of income redistribution with the potential to reduce the negative effects of discrimination (Devens 1988).

Still others claim that a higher minimum wage can fight the negative aspects of the secondary labor market. They state that the increased price of labor will encourage employers to provide more on-the job training in order to appreciate the returns of their higher labor costs. With increased employer provided training and increased monetary incentives to seek stable employment, members of the secondary labor market would be freer to make the transformation into the mainstream of the primary market (Hamermesh 1984).

Another commonly held position is that workers are also consumers. By increasing the minimum wage we are also increasing the amount of money spent by the minimum wage worker. Such increases would quickly translate into increased product demand and lead to general economic expansion.

Costs

An obvious cost of the minimum wage is that it does, in fact, reduce employment. The wide variation in reported job loss effects notwithstanding, we do know that any meaningful increase in the minimum wage will produce some decrease in employment. That decrease may occur as a reduction in hours worked, perhaps as a movement from full-time toward part-time employment, or in actual jobs eliminated. Whatever form it may take, at least some workers will be made worse off by an increase in the minimum wage. Further, a delayed result could be the substitution of production capital for low-skilled labor. Investment in advanced technological production equipment, such as robotics, might become economically preferable to employers facing rising labor costs. In this case many jobs could be lost forever (Hamermesh 1984).

A common argument against raising the minimum wage is that it increases the costs of production and that those costs are ultimately passed on to the consumer in the form of higher prices. A widespread increase in consumer prices would create a circular effect wherein the worker, although making more money, would have relatively no more spending power than before the wages were increased and consumer prices followed. Increases in the minimum wage would therefore be inflationary. Instead of accomplishing its original purpose of helping the worker, the resultant inflation would worsen American balance of payments by reducing foreign consumption of the now higher priced American products. This position states that an increase in the minimum wage would actually be detrimental to the minimum wage worker.

While each of the benefits and costs mentioned here has some merit, the relative importance of each and their individual effects upon the worker and the economy as a whole are the bases of continued debate. This debate is not restricted to the ranks of social and economic theorists, but is pursued actively in a very real-world forum, the United States Congress. Chapter four will address that arena.

CHAPTER FOUR

FEDERAL WAGE POLICY

For a bill to become law it must successfully negotiate the legislative process where there are numerous junctures at which the bill may be killed or drastically altered. Interest groups, often having high stakes in the outcomes, can exert great influence upon the entire procedure and the individual legislators. They do so both formally and informally. Informal methods, such as campaign contributions or the extension of fees for speaking engagements, can often earn the allegiance of individual lawmakers. Because interest groups are also an important source of industry and functional viewpoints, and because they often possess detailed expertise in their areas of concern, they are often called upon to testify in formal hearings in both houses. Interest group influence and manipulation are often described as having preeminent influence on the legislative process (Lowi 1969).

Minimum wage legislation is no exception. The major interests in promoting minimum wage increases are the labor unions. Opposition is generally from coalitions of business interests that would be most affected. These tend to be businesses in highly competitive industries and where payrolls constitute large proportions of total product or service costs, such as described in Chapter Two. The Farm Bureau, American Hotel and Motel Association, and various retail groups are typical of minimum wage opponents. A brief description of the legislative process follows.

The Legislative Process

Bills may be sponsored and introduced in either house by individual Congressmen or by joint submission. Those written in the Executive branch are normally introduced by the chairman of the committee which has jurisdiction. The bill is referred to the appropriate committee where it comes under initial scrutiny and is placed on the calendar. This is the point of sharpest Congressional focus because failure of the committee to act on the bill is equivalent to killing it. The majority of bills that are unsuccessful are killed at this juncture. Bills may be handled by the parent committee but are more often assigned to subcommittees for study and hearings. Such hearings may be closed or public and it is here where most of the evaluation and alteration occur. It is also here where interest groups may exert their formal influence.

After often lengthy consideration the subcommittee reports its findings back to the full committee. The recommendation may be to take no further action on the bill, effectively killing it, or to proceed with action but often with numerous amendments to the original proposal. The full committee then determines its recommendation. If it wishes to proceed toward passage it orders the bill reported to the House or Senate where it is placed on the calendar to be debated and subsequently voted on. Bills are often returned to committee or subcommittee for modification. Following passage of a bill in either the House or the Senate it is sent to the other chamber where it is again subjected to a similar process. Ultimately, through compromise if necessary, both the House and the Senate must agree to a single legislative document before it is sent to the White House for signature. Even having survived the legislative process the law is still subject to Presidential veto. The veto can only be overridden by a two thirds vote in both houses (Congressional Quarterly Guide to Current American Government 1979).

However, even having become law, bills which require funding are still subject to emaciation due to insufficient budgetary support from either the legislature or executive. Other bills, such as one concerning the minimum wage, can be subjected to less than enthusiastic implementation or enforcement by the bureaucracy. In this case the only recourse would be through strong Presidential leadership or action by the Judiciary (Cobb and Elder 1983).

Powerful and determined interest groups can exert their influence through every step of the entire process. A review of recent minimum wage legislative initiatives is provided in the next section.

Minimum Wage Legislation

The Reagan Administration was typically conservative in condemning the minimum wage as a constraint to greater employment opportunity. The President suggested in 1983 that the minimum wage had "priced a number of people and jobs out of existence." (Congressional Digest 1985, 64:105). Upon his request, Representative Barber B. Conable, Jr., NY, R. and Senator Robert J. Dole, KS, R. introduced companion FLSA amendment proposals to the Congress which provided for a youth subminimum wage. Unlike the interim subminimum wage allowances made in 1961 and 1966 in conjunction with expansion of coverage, youth subminimum programs are designed to become permanent. The rationale for such action is to provide increased employment opportunity for young people with little employment experience and few skills.

The 1983 measures were referred to the House Committees on Ways and Means and Education and Labor and in the Senate to the Finance Committee. No action was taken by the committees and the proposals were therefore killed in both chambers.

In May of 1984, again in response to Presidential initiative, a modified version of the Conable/Dole bill was presented by Senator Charles H. Percy, IL, R. and Representative Ron Packard, CA, R. The proposals were referred to the Senate Labor and Human Resources Committee and to the Education and Labor Committee in the House. President Reagan's message to the Congress was, in part:

> Studies over the past decade have repeatedly demonstrated that the minimum wage has reduced job opportunities for large numbers our youths. (64:128).

In the Senate hearings that followed, James G. O'Hara, Chairman of the Minimum Wage Study Commission created by the 1977 FLSA amendment, was called to testify. Mr. O'Hara complained that the conservative sponsors had exaggerated and misapplied the data which were contained in the study commission report. In testimony he also stated the following:

> If suggestions were made that the very real problems of women or members of minority groups should be solved by paying them less for their labor, such a proposal would be rejected out of hand as fundamentally unjust. (64:127).

Although the Percy/Packard bill was pushed hard by the Administration as well as by business interest groups, no further action was taken and the subminimum wage proposal failed in the 98th Congress.

The 1983 and 1984 rounds were attempts by the conservatives to weaken the FLSA through subminimum wage provisions. In the 99th Congress of 1985-1986 a bill was introduced by the Democrats to raise the minimum wage. The Republicans also tried again but this time their bill would have eliminated it altogether. Both initiatives resulted in no action from the responsible committees and they fell by the wayside.

Senator Edward M. Kennedy, MA, D., Chairman of the Committee on Labor and Human Resources, introduced the Minimum Wage Restoration Act of 1987 to the 100th Congress. A companion bill was simultaneously submitted in the House by Representative Augustus F. Hawkins, CA, D., Chairman of the Committee on Education and labor. The proposed legislation would have increased the minimum wage to $3.85 in 1988, to $4.25 in 1989, and to $4.65 in 1990. The hearings were conducted April through July of 1987. Testimony in favor of the increase was received from the AFL/CIO, the Amalgamated Clothing and Textile Workers' Union, and the International Ladies' Garment Workers' Union. Opponents testifying included the American Farm Bureau, the American Hotel and Motel Association, the Manufacturing Jewelers and Silversmiths of America, and a prominent business leader, John R. Glennie. In typical fashion, the business groups quoted various economic studies alluding to the number of jobs that would be lost as well as the inflationary impact of raising the wage floor. The unions countered with studies of their own which minimized the negative economic effects and stressed the minimum wage as necessary to provide a decent standard of living as well as its potential to reduce welfare costs (Congressional Digest 1987,66).

The measures were approved by committee in both houses and went to the floor of the House in May and to the full Senate in September of 1988. Debate in both houses consisted largely of the same rhetoric presented at the hearings in committee as well as proposals and counter-proposals for amendments. Split along nearly partisan lines, the bill became stalled in the House in mid-summer and failed to come to a vote in the Senate by late September (Lawrence 1988) (Morehouse 1988).

Meanwhile George Bush, the Republican presidential nominee, departed from the Reagan Administration's hard line by announcing that he would support a modest increase in the minimum wage if it were tied to a lower training wage for new workers. In March of 1989 Elizabeth Dole, President

Bush's new selection as Secretary of Labor, announced the new administration's position. The President would accept a stepped increase in the minimum wage of 90¢ over three years to $4.25 by 1992. The increase was contingent upon a subminimum training wage of $3.35 that would apply to new hirees for the first six months of employment. The Democrats, led by Senator Kennedy, attacked the Bush proposal as being too small as well as vigorously opposing the subminimum provisions. Secretary Dole countered that the President would hold the line at his original offer and veto any legislation that went beyond those stipulations. The Democrats in the House, however, with agreement of the labor unions, agreed to compromise by reducing their opposition to the training wage but insisted that it apply only to new hirees with no previous work experience. They also agreed to a slight reduction in the dollar figure to $4.55 by 1991. The House bill was approved by a vote of 248-171 on March 23rd.

As of mid-April the measure is still being considered in the Senate where there is a great deal of contention over the subminimum training wage. The Republicans insist that it is necessary to protect business from the overall impact of the wage increase. The Democrats argue that the applicability of the training wage to all new employees, rather than just to those without previous work experience, could lead to hire-and-fire strategies by minimum wage employers negating the benefit of the higher wage. What the final resolution in the Senate will be is unknown at this time but it is expected that the Democrats will at least place some constraints on the subminimum wage similar to those of the House. Nevertheless, President Bush is still holding adamantly to his pledge to veto any measure which goes beyond his original offer (Grand Forks Herald, March-April 1988).

The minimum wage amendment has become one of the first serious conflicts to arise between the new Administration and the Congress. Whatever the Senate agrees to must be eventually resolved in Joint Committee with the House before going to the President. It is unlikely that the final product of the Legislature will be a bill that meets the President's conditions, especially since the House has already gone beyond them. In this early test of the Administration's resolve, it is also unlikely that the President will back down on his ultimatum. That would set an uncomfortable precedent. If there is insufficient support in either house for an override of the veto, the likelihood of a minimum wage increase becoming law this year appears doubtful.

The battle-lines are clearly drawn, the Democrats and the labor unions versus the Republicans and business interests. The inability of the opponents to compromise on current legislation appears certain. What is needed is a new minimum wage proposal that will allow compromise in other areas rather than just the current issues of dollar amount and the subminimum contingency. Just such a proposal is presented in the next chapter.

CHAPTER FIVE

RECOMMENDATION

Conclusion

The Great Depression of the 1930's signalled the final demise of the philosophy of Social Darwinism. It was a period during which millions of middle class Americans, not just the lazy and the unfit, became acutely aware of the meaning of poverty. A new philosophy, that government played a role in the economic well-being of its citizens, emerged. The Fair Labor Standards Act was one of the ramifications of the new philosophy. Intended to protect the American worker and to provide a decent return on his labor, the Act has endured to the present day. Nevertheless, it also remains a controversy between liberal and conservative values and continues to create extensive debate. Coverage under the Act has been expanded periodically as has the minimum wage itself. Major expansion of coverage occurred in 1961 and 1966 and in both cases a four to five year subminimum wage was provided to allow newly effected businesses to adjust. Today, roughly ninety percent of nonsupervisory jobs are covered. Traditionally the minimum wage has been set at roughly fifty percent of the average hourly wage of nonsupervisory workers. The last adjustment to the wage was in 1981 when it was set at $3.35 an hour. Since 1981 increases in the cost of living and general wage escalation have reduced the minimum wage to less than thirty eight percent of the national average, its lowest level in forty years. While about ninety percent of nonsupervisory workers are subject to the minimum, some ten percent remain in the uncovered sector. That sector consists of industries which typically are highly competitive and with labor costs constituting high percentages of final product prices, such as retail and service industries. While the Federal government has not produced new minimum wage legislation since 1981, the individual states have been active. All but nine states now provide their own worker protections, eighteen have universal coverage, and ten require wages above the Federal minimum.

Orthodox economic wage theory, through the effects of supply and demand, has shown that there is a negative relationship between wages and employment. To make valid predictions based on orthodox theory it is necessary to use reliable elasticity estimates. Several studies have been conducted which have yielded a wide range of results. The liberals or conservatives have had only to select those results which reflect their differing ideological viewpoints. The job rationing model suggests that the size of the covered sector relative to that of the uncovered sector is also important in determining the results of a mandated wage increase. However, neo-classical theories question the reliability of orthodox prediction because of the effects of seniority provisions, wage rigidity, and the existence of an unmotivated and untrained secondary labor market. The easily manipulated application of orthodox theory leaves many unanswered questions, such as, does an overall increase in the income of job keepers offset the normally smaller overall loss to job losers? While economic theory can provide general guidelines to understanding the minimum wage, it cannot be a substitute for the normative judgements that are essential to equitable resolution.

As the FLSA was born of the Great Depression, so was the concept of government largesse for the needy, welfare. The minimum wage can be an effective instrument to decrease the cost of welfare. The debate is essentially one of determining who is to pay for that largesse, the taxpayer or industry. Low, or nonexistant, minimum wages can act as a subsidy to low wage employers at the expense of the public. Higher minimum wages can shift the responsibility back to industry and provide greater employment incentive to workers. Nevertheless, a higher wage floor will result in some increase in unemployment and can contribute to inflationary pressure. What is needed is a determination of the right mix of government subsidy and industry responsibility. That determination must necessarily be made by the Legislature.

The legislative process is one that is subject to considerable influence by powerful interest groups. Business and labor interests continually vie for the attention of the legislators and achieving the right mix is essentially a process of balancing those interests. During the Reagan Administration the conservative ideology had the upper hand. The new Administration is prepared to grant concessions but they are far short of what the liberals are demanding. Recent Democratic attempts in the Congress to raise the wage floor have resulted in extensive debate and will probably be thwarted by President Bush's hard-line position. What is needed now is a new approach to minimum wage legislation, an approach providing more leeway for compromise between the adversaries, and one that will enhance the benefits of the FLSA without severely constraining the growth of the economy.

A New Approach

While it appears that the minimum wage is overdue for an increase, an inequitable situation also exists by not having universal coverage. Those industries which are not subject to the law are being subsidized by both the taxpayer, through higher welfare costs, and the unskilled employees themselves who have little choice of their employer. Although the increased costs to such employers would ultimately be paid by the consumer, that would be far more equitable than the present arrangement. As the situation presently exists, many employers are already paying above the Federal minimum, partially due to state laws and partially due to localized labor demand. Now, while the wage rates are low, is the perfect time to expand the coverage. If wage rates are allowed to increase before such expansion, it would be increasingly expensive for newly covered employers and therefore much more difficult to achieve. In addition to more equitably assigning responsibility to the uncovered areas that are currently subsidized, expansion to universal coverage would also eliminate the negative aspects of the job rationing scenario. It could also simplify enforcement procedures through removal of most of the exceptions. Further, it presents a very real possibility of decreasing the ingrained traits of the secondary labor market by bringing it into the mainstream of primary employment practices.

The specific proposal is to expand the coverage of the FLSA to all employees with very limited exceptions. Those who are self-employed could not be effectively included for they are self-employed by choice. Also, current allowances for tipped employees and for handicapped workers in sheltered workshops appear to be equitable and should be maintained. The current exemption which allows for full-time student employment at subminimum wages in selected industries should be maintained but it should be altered to include all industries. The program appears to be a benefit to students who only require part-time or temporary employment. There is, however, no reason to limit such employment to only agriculture, retail, or higher education. It would be necessary to maintain and expand current subminimum student certification procedures to preclude possible widespread abuse. As in past expansions of coverage, newly covered employers should be granted subminimum authority for up to five years to allow for industry adjustment.

It appears unlikely that, under a Republican President, the Democratically controlled Congress will succeed in achieving its desired amount of increase in the minimum wage for at least the next four years. Furthermore, the Administration has tied even modest increases to the stipulation of a subminimum training wage. It is therefore recommended that the liberal coalition considerably reduce the size of its rate increase demands. Instead, it should attempt to trade that increase for a concession in expanded coverage. In the absence of what appear to them to be unreasonably high rate demands, the conservatives would be less inclined to hold fast to their training wage stipulation. It is entirely possible that by acceding to conservative pressures on the dollar amount, that the liberals may be able to make important advances in the area of coverage. It may be to the American worker's advantage to make that move now and to postpone large increases in the minimum wage until such time as it becomes politically promising.

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