

Will a \$15 Minimum Wage Hurt Small Businesses?

Locality-based wages may be one solution

By Roy Maurer

March 16, 2021

Small businesses have been especially hard-hit during the COVID-19 pandemic. That's why some believe this is an inopportune time to pursue raising the federal minimum wage to \$15 an hour by 2025, as Democrats in Congress have proposed. But advocates of the Raise the Wage Act say that lower-income workers have also been struggling during the pandemic and the federal minimum wage is long-overdue for an increase.

The introduction of the legislation resets the stage for debating the challenges and benefits of raising the minimum wage (www.shrm.org/hr-today/news/hr-news/pages/federal-minimum-wage-increase-good-for-business-cost-too-much.aspx) and the impact the policy would have on small employers.

The federal minimum wage was last raised—to \$7.25—in 2009. Just over 1 million workers earned wages that were at or below the minimum wage in 2020, according to the Bureau of Labor Statistics.

A Tradeoff

The dilemma facing federal lawmakers was expressed by Rep. Dean Phillips, D-Minn., during a recent hearing on the issue called by the House Committee on Small Business.

"According to the Congressional Budget Office, the [Raise the Wage Act] will likely raise wages for 27 million Americans, raise almost a million people out of poverty, and increase aggregate wages for low-wage workers by over \$300 billion over the next decade," he said. "Unfortunately, the same study also projects that this policy could cost 1.4 million jobs ... and the loss of some small businesses."

Phillips said he hears the concerns from constituents like the owner of The Original Pancake House in Plymouth, Minn. "Like so many businesses which rely on public gathering to succeed, his is barely hanging on. His restaurant—like all restaurants—runs on thin margins during the best of times, and he is deeply concerned that a \$15 minimum wage will mean he will have to cut jobs if he hopes to stay open."

Rep. Elizabeth Ann Van Duyne, R-Texas, said she couldn't think of anything more devastating to small businesses as they try to recover from the economic effects of the pandemic. "Small business owners have told me that increasing the minimum wage will have a disastrous impact on them," she said. "Many said they would have to close their doors immediately, and others said they would have to choose between shutting down or replacing their workers with automation."

Phillips said he believes there are ways to "mitigate the negative impacts of such a policy while maximizing the positive impacts of raising wages for millions of Americans."

Job Losses, Business Closures

Opponents of increasing the minimum wage to \$15 argue that it will burden small businesses—which make up 99 percent of all employers—with increased labor costs and result in layoffs, expediting automation, or going out of business.

"Employers cannot have their labor costs increase by up to 100 percent without significant disruptions to their operations," said Rachel Greszler, a research fellow at the Heritage Foundation in Washington, D.C. "Responses to a \$15 federal minimum wage will vary depending on their industries and unique circumstances, but their options include eliminating positions, cutting employee hours, reducing benefits, automating or outsourcing jobs, or closing down."

Greszler added that even employers of middle-wage workers may be subject to wage pressure. "In order to attract and retain the workers they need, employers have to maintain a hierarchy of wages based on experience and productivity—they cannot pay shift managers the same rate as entry-level workers."

Ian MacLean, the owner of Highland Landscaping in Southlake, Texas, and chair of the U.S. Chamber of Commerce Small Business Council, said that his company's lowest-wage earners currently make \$11 per hour. "If the lowest-wage earners are increased to \$15 per hour, every one of my employees currently making \$15 per hour or more would, justifiably, want their hourly rates increased commensurate with their skills, experience and tenure above the new \$15 per hour employees."

Greszler noted that some employers will respond to an increase in the minimum wage by replacing low-income workers with machines.

MacLean agreed that to mitigate the effects of a minimum wage hike to \$15, "we would fast-track automation solutions and eliminate most of our entry-level and lesser-skilled labor positions."

"These small businesses are the same as households," Greszler said. "If we were faced with paying twice the rent or twice the mortgage, we would have to make adjustments. Small business owners tell me that they're taking out lines of credit during this pandemic because they care so much about their workers and they don't want to lay them off."

Higher Retention, Productivity

Proponents of the wage increase say that it will return low-wage workers to a standard of living considered the bare minimum decades ago, turning back the erosion of the value of the minimum wage after inflation.

Those making the federal minimum wage now make 30 percent less in inflation-adjusted pay than federal minimum wage workers did 53 years ago, said Heidi Shierholz, senior economist and director of policy at the Economic Policy Institute in Washington, D.C.

"Had the minimum wage kept pace with labor productivity growth since 1968, the minimum wage would have been \$21.69 in 2020, and ... would be \$23.53 in 2025," she said. "Affected workers who work year-round would earn an extra \$3,300 a year—enough to make a tremendous difference in the life of a supermarket clerk, home health aide or fast-food worker who today struggles to get by on less than \$25,000 a year."

The Raise the Wage Act also indexes the minimum wage to median wages. "By establishing regular, predictable increases to the minimum wage that are linked to overall wage growth, the proposed legislation improves the ability of the minimum wage to reduce inequality," Shierholz said. "A rise to \$15 an hour would reverse decades of growing pay inequality between the lowest-paid workers and the middle class, and indexing future increases would prevent any future growth in that gap."

She added that multiple studies also show that a higher minimum wage would benefit employers by boosting morale and productivity and decreasing employee turnover and absenteeism.

That's what Punch Neapolitan Pizza co-owner John Puckett is counting on. The St. Paul, Minn.-based pizza chain currently pays an average of \$13 per hour for starting wages and plans to move to \$15 per hour by 2022, as directed by city mandate.

"We're trying to figure it out," Puckett said of the impact of the rising minimum wage on his business. "One of our key business strategies has been to recruit and hire the best employees, and central to that strategy has been paying more than our competitors and well above legal minimums to ensure we attract and retain the best people," he said. "Employee retention is about two and half times longer than industry average," he added.

Paying workers higher minimum wages is a priority for the company but does come at a cost, he said. "Our store-level labor cost is significantly higher than industry average. But since our business strategy is not to maximize short-term profit but to build a company that will last generations, we think the extra money we spend on labor is money well-spent."

Locality-Based Pay

Some on both sides of the aisle agree that a single, nationwide federal minimum wage may not be the best solution. "Different regions with different economic conditions should not have the same wage policy," said Ryan Young, a senior fellow at the Competitive Enterprise Institute in Washington, D.C.

That's because of the widely varying cost of living across different parts of the country. "In high-cost Manhattan, for example, these tradeoffs may barely be visible at a \$15 minimum wage, because wages there are already in that range," Young said. "In smaller towns where costs and wages are lower, the tradeoffs would be severe."

In Mississippi, for example, \$15 per hour is the median wage. "Imposing a \$15 minimum wage on Mississippi would be like imposing a \$35.74 minimum wage on Washington, D.C., the equivalent of more than \$74,000 per year," Greszler said.

She added that the best solution would be to use a locality-based wage system tied to the median wage, taking care not to disproportionately impact lower-cost areas negatively.

"States and cities are free to set their own policies, and most already have," Young said. "Twenty-nine states currently have minimum wages well above the current federal minimum, and many cities have their own citywide minimum wages beyond state requirements that don't impose on communities with lower living costs."

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