

## Minimum Wage and Other Income Supplements

### ISSUE

This *Issue Review* examines the current situation of State and Federal Minimum Wage Laws. Also examined are the Federal and Iowa Earned Income Tax Credit and other income tax policies and assistance programs aimed at supplementing incomes.

### AFFECTED AGENCIES

Iowa Workforce Development, Department of Human Services, Department of Revenue

### CODE AUTHORITY

Iowa Code chapter [91D](#) and section [422.12B](#)

### MINIMUM WAGE

The minimum wage, established by federal law in the [Fair Labor Standards Act](#) (FLSA) and State law in Iowa Code chapter [91D](#), is currently set at \$7.25 an hour. The State of Iowa last raised the State minimum wage in 2007, reaching \$7.25 on January 1, 2008, and the federal minimum wage reached this same level in 2009. Application of the minimum wage law always goes to the more stringent statute. The federal and State minimum wage law applies to most hourly wage earners employed in Iowa. Most small retail and service establishments grossing less than \$300,000 annually are not required to pay the minimum wage. Employers may pay an initial employment rate of \$6.35 for the first 90 calendar days of employment. There is a tip credit for tipped employees that customarily and regularly receive more than \$30.00 a month in tips. They must be paid at least \$4.35 per hour. Exempted employees from the FLSA and Iowa Code chapter [91D](#) include executive, administrative, and professional employees; outside sales employees; employees in certain computer-related professions; employees in certain seasonal amusement or recreational establishments; employees of certain small newspapers; seamen employed on foreign vessels; employees engaged in fishing operations; employees engaged in newspaper delivery; farmworkers; and casual babysitters.

In 2014, 22 states and the District of Columbia (D.C.) have state minimum wage levels that are higher than the federal minimum wage. Nineteen states, including Iowa, have minimum wage levels the same as the federal level, four states have minimum wage levels below the federal level (the federal minimum consequently overrides), and five states have not established a state minimum wage.<sup>1</sup> So far in 2014, 10 states and the D.C. have enacted minimum wage increases, four states approved minimum wage increases through ballot measures, and Illinois

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<sup>1</sup> National Conference of State Legislatures. State Minimum Wages *available at* <http://www.ncsl.org/research/labor-and-employment/state-minimum-wage-chart.aspx> (last visited December 8, 2014).

voters approved a ballot advisory measure. Additionally, Oklahoma has enacted legislation that prevents any municipality from increasing the local minimum wage.

Thirteen states and the D.C. have minimum wage levels that are linked to a consumer price index, causing the minimum wage to be adjusted on an annual basis. Of those states, nine will see increases effective January 1, 2015. Three states and the D.C. have provisions that prevent the state minimum wage from equaling the federal minimum wage by adopting an increase by reference.

Minimum wage, at both the State and federal level, is referenced throughout Iowa Code. For example:

- Iowa Code section [49.20](#) requires members of each Precinct Election Board to be paid no less than the State minimum wage, unless the members voluntarily offer to serve without pay.
- Iowa Code section [99F.7\(7\)](#) states that it is the intent of the General Assembly that employees of licensed casinos in the State be paid at least 25.0% above the federal minimum wage (currently calculated to be \$9.06).
- Iowa Code section [909.3A](#) provides that community service can be used to pay a fine assessed by the courts, and is calculated at the rate of either federal or State minimum wage, whichever is higher.

## **CURRENT SITUATION**

### **Current Statistics**

The U.S. Bureau of Labor Statistics estimates that in 2013, a total of 921,000 workers in Iowa were paid an hourly wage, and 50,000 of these workers earned wages equal to or less than the prevailing federal minimum wage.<sup>2</sup> This represents 5.4% of all workers paid hourly rates in Iowa, compared to 4.3% nationally and 4.4% in the Midwest. The same survey also documented some of the following national characteristics about workers with earnings at or below the federal minimum wage:

- **Age:** Workers age 16 to 19 make up 24.2% of minimum wage workers earning at or below the federal minimum wage. Expanding that to workers age 16 to 24 increases the total to 50.4% of those working at or below the federal minimum wage. The percentage grows to 71.7% when looking at workers age 16 to 34. Workers older than age 55 make up 8.1% of those at or below the minimum wage.
- **Education:** Workers holding less than a high school diploma make up 28.1% of workers at or below the federal minimum wage, 29.7% of workers are high school graduates with no college education, and 34.3% of workers have some college or an associate's degree.
- **Occupation (type of work):** Of workers at or below the federal minimum wage, 63.6% are employed in Service Occupations, primarily in food preparation and serving. Sales and Office Occupations ranked second at 20.5%.
- **Industry: Of all the workers age 16 and older paid hourly rates at or below the minimum wage:**
  - Leisure and Hospitality workers make up 55.0% of the total. That represents 19.0% of that specific industry sector.
  - Wholesale and Retail Trade workers make up 14.8% of the total. That represents 3.9% of that specific industry sector.
  - Manufacturing workers make up 2.8% of the total. That represents 1.1% of that specific industry sector.

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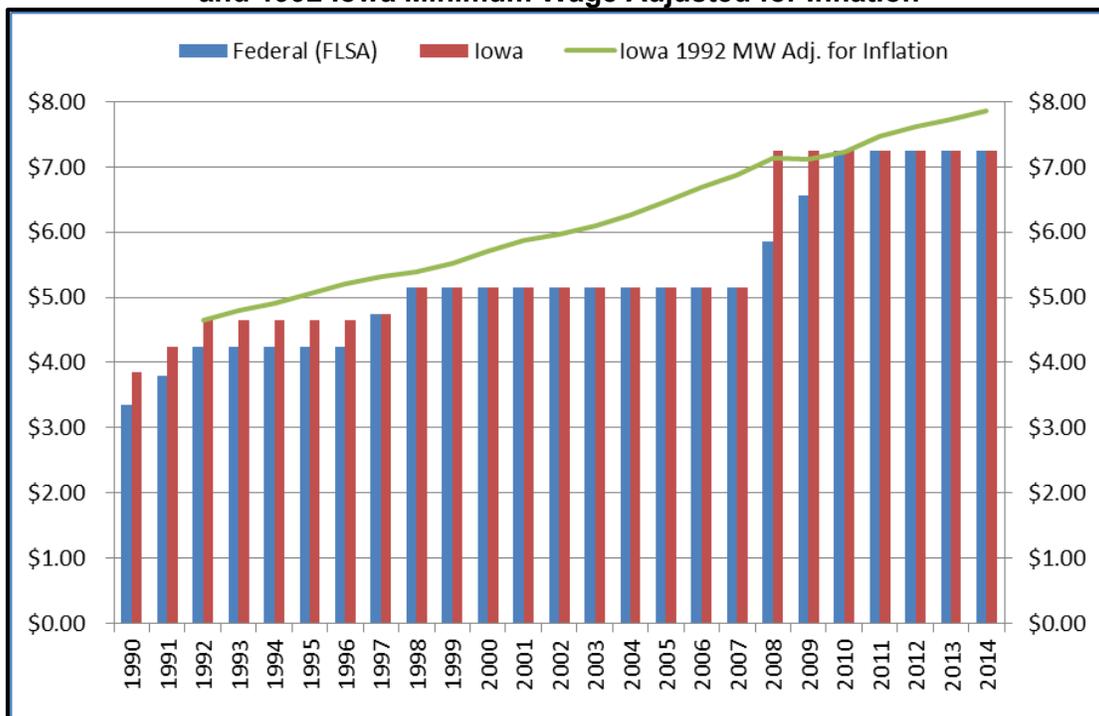
<sup>2</sup> U.S. Bureau of Labor Statistics. Characteristics of the Minimum Wage Worker 2013, (February 2014), available at <http://www.bls.gov/cps/minwage2013.pdf> (last visited May 22, 2014).

- **Hours Worked:** Regarding hours worked per week for workers at or below the minimum wage, 30.5% are estimated to work at least 35 hours or more per week and 22.0% are estimated to work 40 hours or more. Work weeks of less than 35 hours represent 57.4% of workers.
- **Marital Status:** Of the workers at or below the federal minimum wage, 66.8% have never married and 20.7% are married with their spouse present.

**Historical Context**

Iowa’s first minimum wage was enacted in 1989 Iowa Acts, chapter 14 starting at \$3.85 per hour on January 1, 1990, and was fully phased in at \$4.65 per hour on January 1, 1992. The 1992 federal minimum wage was \$4.25, \$0.40 lower than the Iowa minimum wage. Iowa Code adopts the federal minimum wage by reference when it exceeds the Iowa minimum wage and the federal minimum wage overrode the Iowa minimum wage from 1996 until 2007, when the Iowa minimum wage was increased. **Chart 1** examines the Iowa minimum wage, federal minimum wage, and the 1992 Iowa minimum wage when adjusted for inflation using the Consumer Price Index (CPI). The minimum wage rate displayed reflects the wage in effect on January 1 of each year and does not account for increases that took place in the middle of the year. After adjusting for inflation, the Iowa minimum wage enacted in 1989 that became effective in 1992 would be worth \$7.86 per hour in 2014, \$0.61 higher than the current level.

**Chart 1. Minimum Wage on January 1, 1990-2014 and 1992 Iowa Minimum Wage Adjusted for Inflation**



**Source:** U.S. Department of Labor, Iowa Code, and Legislative Services Agency (LSA) calculations utilizing U.S. Bureau of Labor Statistics data ([http://www.bls.gov/data/inflation\\_calculator.htm](http://www.bls.gov/data/inflation_calculator.htm)).

**Note:** Represents the minimum wage in effect on January 1 and does not show mid-year increases.

**EARNED INCOME TAX CREDIT**

The federal Earned Income Tax Credit (EITC) was created in 1975 and made permanent in 1978. The credit was expanded in 1986 and revised in 1990 and 1995. This is a refundable tax credit that provides cash assistance to lower-income working parents and individuals through the tax system. Anyone wanting to claim the EITC must file an annual income tax return to receive the benefit. The amount of the tax credit depends on age, the amount of earned income, adjusted gross income, and qualifying children.

The EITC is designed to increase with earnings up to a maximum credit benefit; remains at the maximum credit amount for a certain range of incomes; and then begins to phase out at other income levels until it decreases to zero. **Table 1** below outlines the features of the EITC for 2014. "Earned Income Amount" represents the earned income at or above which the maximum credit amount is available. Since 1987, all of the components of the EITC are indexed to the Consumer Price Index and therefore are adjusted annually.

**Table 1. 2014 Federal and Iowa Earned Income Tax Credit**

	No Children	One Child	Two Children	Three or More Children
<b><u>Earned Income Tax Credit</u></b>				
Maximum Federal Credit	\$ 496	\$3,305	\$ 5,460	\$ 6,143
Maximum Iowa Credit	74	496	819	921
<b>Total</b>	<b>\$ 570</b>	<b>\$3,801</b>	<b>\$ 6,279</b>	<b>\$ 7,064</b>
<b><u>Earned Income Tax Credit Parameters</u></b>				
Earned Income Amount for Maximum Credit	\$ 6,480	\$9,720	\$ 13,650	\$ 13,650
Threshold Phase-out for Single and Head of Household	8,110	17,830	17,830	17,830
Credit Completely Phases Out for Single Head of Household	14,590	38,511	43,756	46,997
Threshold Phase-out for Married Filing Jointly	13,540	23,260	23,260	23,260
Credit Completely Phases Out for Married Filing Jointly	20,020	43,941	49,186	52,427

**Sources:** U.S. Department of the Treasury, Internal Revenue Service. *Internal Revenue Service Bulletin*, Bulletin No. 2014-47. p. 540. (<http://www.irs.gov/pub/irs-irbs/irb13-47.pdf>) and LSA calculations.

**Note:** A tax filer with no children must be at least 25, but not more than 64 years old, to claim the federal credit.

Twenty-four states and the D.C. have some form of EITC for state income taxes (nine states do not levy an individual income tax on wages and salaries). Most are based on the federal credit, some are refundable, and others are not.<sup>3</sup> Iowa first enacted an EITC that was equal to 5.0% of the federal credit and nonrefundable with 1989 Iowa Acts, chapter [268](#) (State Individual Income Tax Act). In 1991, the credit rate was increased to 6.5% and in 2007 the credit rate was increased to 7.0% and made refundable. The credit was increased to 14.0% in tax year 2013, and in 2014 is equal to 15.0% of the federal EITC.<sup>4</sup>

According to the Iowa Department of Revenue (DOR), in 2009, a total of 208,342 households claimed \$28.5 million of Iowa's EITC.<sup>5</sup> According to preliminary DOR estimates, in 2013 a total of 221,071 households claimed \$65.4 million of Iowa's EITC.<sup>6</sup>

<sup>3</sup> A refundable tax credit is not limited by the total tax liability of the filer, allowing for a refund of the amount above the tax liability. A nonrefundable tax credit is limited by the total taxes owed and any excess is forfeited.

<sup>4</sup> 2013 Iowa Acts, ch. [123](#), §70, State and Local Taxation of Property and Income Act.

<sup>5</sup> Iowa Department of Revenue. "Iowa's Earned Income Tax Credit Tax Credits Program Evaluation Study," (Revised February 2012), available at [https://tax.iowa.gov/sites/files/idr/EITC2011\\_revised.pdf](https://tax.iowa.gov/sites/files/idr/EITC2011_revised.pdf) (last visited December 9, 2014).

<sup>6</sup> Iowa Department of Revenue. "Tax Credit Contingent Liabilities Report," (December, 2014).

## **OTHER INCOME SUPPLEMENTS**

Some benefits that a minimum wage worker may qualify for are outlined in this section. Eligibility for an assistance program does not rely on the hourly wage of a worker, but rather the total monthly income (gross or net depending on the program), that would be impacted by the number of hours worked and the number of jobs held. Other benefits available may only cover very specific categories of situations that involve having a child, the age of the child, or vary depending on where the minimum wage worker lives.

In both the federal and [Iowa income tax](#) structures, there are a number of [tax credits](#) available that are designed to either incentivize certain behaviors or actions within the economy or reduce the tax burden for those in certain circumstances. Some of these tax credits are refundable, some are not. Depending on the type of tax credit available, the tax filer may need to take additional actions such as keeping receipts on certain expenses.

### **Tax Credits**

**Child Tax Credit:** This federal tax credit was created in 1997 and currently provides a tax credit of \$1,000 per child. It has also been made refundable through 2017, referred to as the **Additional Child Tax Credit**, and is refundable for a taxpayer that has earnings of at least \$3,000, with the credit equal to 15.0% of earnings above \$3,000, up to the maximum of \$1,000 per child.

**Child and Dependent Care Credit:** This federal tax credit is provided for the cost of care paid for dependents, mostly children. The maximum rate of the credit is 35.0% for all costs expended and capped at \$3,000 for one dependent and \$6,000 for two or more dependents. The credit is also reduced when a taxpayer's adjusted gross income is above \$15,000.

**Iowa Child and Dependent Care Credit:** This Iowa tax credit is available to filers with income below \$45,000 with qualifying child care expenses. The credit is calculated as a percentage of the federal credit based on the income of the filer.

**Iowa Early Childhood Development Tax Credit:** This Iowa tax credit is equal to 25.0% of the first \$1,000 of expenses paid for early childhood development for children between three and five years of age. The credit is only available to taxpayers with net income less than \$45,000 and cannot be claimed if the Child and Dependent Care Credit is claimed.

**Taxpayers Trust Fund Credit:** This is a nonrefundable tax credit for Iowa taxpayers that timely filed Iowa individual income tax returns and the amount is based on the funds available in the Taxpayer Trust Fund (TTF). It was created in 2013 and was initially funded with \$120.0 million. In tax year 2013, the TTF Credit was the lesser of \$54 for a single taxpayer and \$108 for a married couple, or the net tax liability after accounting for all other tax credits. The credit amount for 2014 has not yet been determined.

### **Assistance Programs**

**Food Assistance:** Formerly known as Food Stamps and also known as Supplemental Nutrition Assistance Program (SNAP), this federal Program helps people with low income and few assets to buy food. The amount of the monthly benefit depends on the number of people in a household and income after deductions. Variations in an individual's income and additional deductions for allowable expenses change the monthly benefit. Income limits and allotment levels for recipients are adjusted annually with the start of a new federal fiscal year each October. The basis for the adjustments is the [U.S. Department of Agriculture Cost of Food, Thrifty Food Plan](#).

**Child Care Assistance:** The [Child Care Assistance](#) (CCA) program was established in 2000 and is administered by the Iowa Department of Human Services. The CCA program subsidizes child care costs for low-income families with working parents, parents gaining work skills,

parents going to school, and parents unable to care for children for a limited time due to physical or mental illness.

Public Housing Assistance Program: Public housing was established to provide decent and safe rental housing for eligible low-income families, the elderly, and persons with disabilities. There are a number of [programs](#) administered by the U.S. Department of Housing and Urban Development that are managed by local Public Housing Agencies (PHAs). One of the better known programs is the [Housing Choice Vouchers](#) (formerly known as Section 8) that allow low-income families to select and lease or purchase privately-owned rental housing. In general, the family's income may not exceed 50% of the median income for the county or metropolitan area in which the family chooses to live. The PHA calculates the maximum amount of housing assistance allowable. The maximum housing assistance is generally the lesser of the payment standard minus 30.0% of the family's monthly adjusted income or the gross rent for the unit minus 30.0% of monthly adjusted income.

Family Investment Program: The [Family Investment Program](#) (FIP) is administered by the Department of Human Services (DHS) and is Iowa's cash assistance program under the federal Temporary Assistance for Needy Families (TANF) Block Grant. The Program provides cash assistance to low-income families with children and provides services that are designed to help those families become self-sufficient. To be eligible for the FIP Program, individuals must meet all income and asset requirements, be a resident of Iowa, and be a U.S. citizen or legally-qualified noncitizen (such as refugees). The Program has a 60-month lifetime benefit limit with exceptions in cases of hardship.

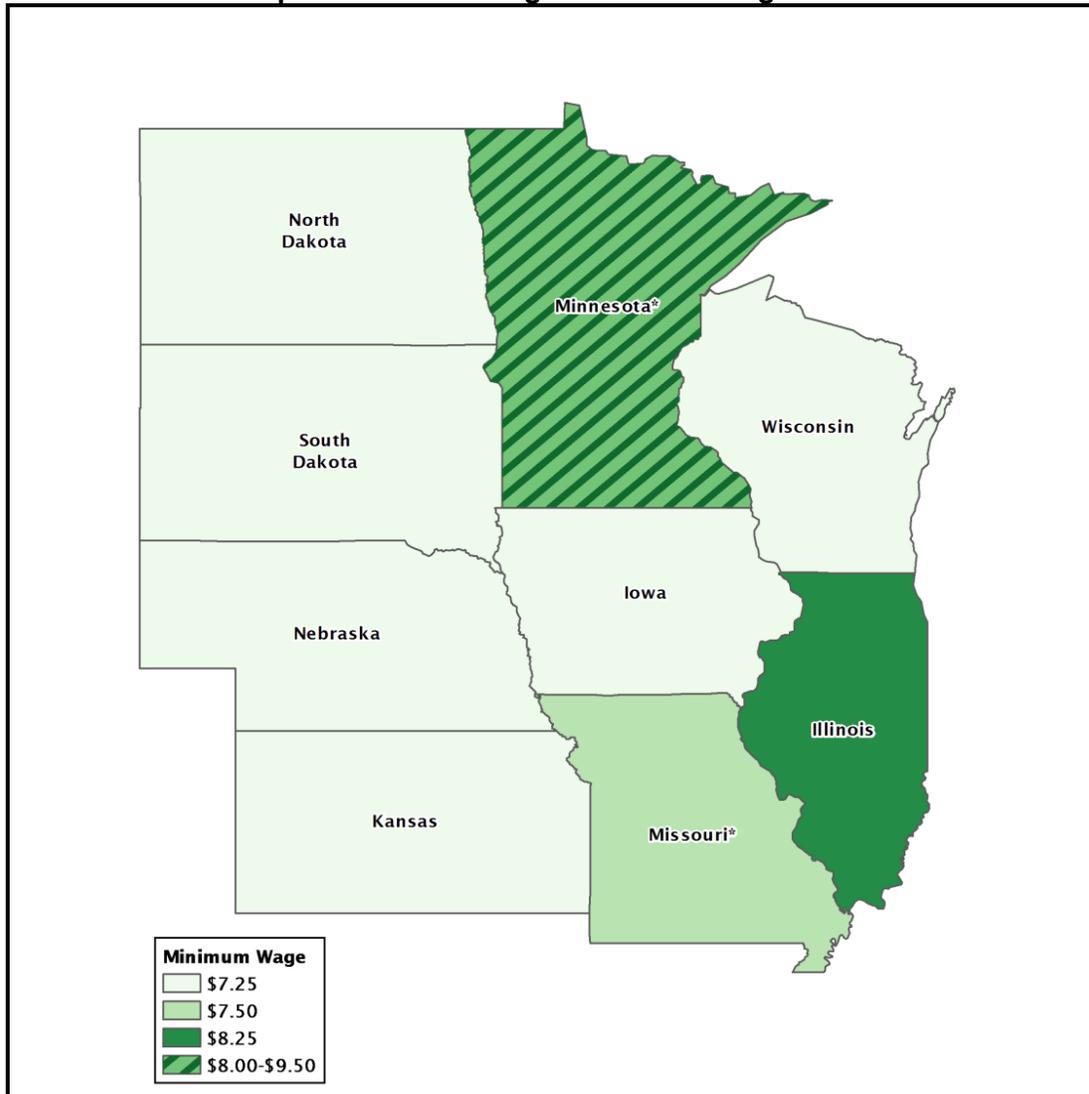
Low Income Home Energy Assistance Program: This Program is a federally-funded block grant program designed to aid qualifying households in the payment of a portion of their residential heating costs for the winter heating season.

This *Issue Review* does not consider health care benefits and subsidies. For a further review of some of the previously highlighted programs and their eligibility and impacts, see the *Legislative Guide* [FIP, Food, and Child Care Assistance](#).

## **MINIMUM WAGE AND EITC IN OTHER STATES**

Missouri was the first state in the Midwest to adopt a cost-of-living increase factor starting in January of 2008 and now annually adjusts the minimum wage based on this factor. Minnesota will begin indexing increases to the minimum wage in 2018 after the final scheduled increase takes effect in August 2016. To present a full regional view of current policy, **Map 1**, on the following page, outlines the minimum wage in surrounding states.

**Map 1. Minimum Wage in Surrounding States**

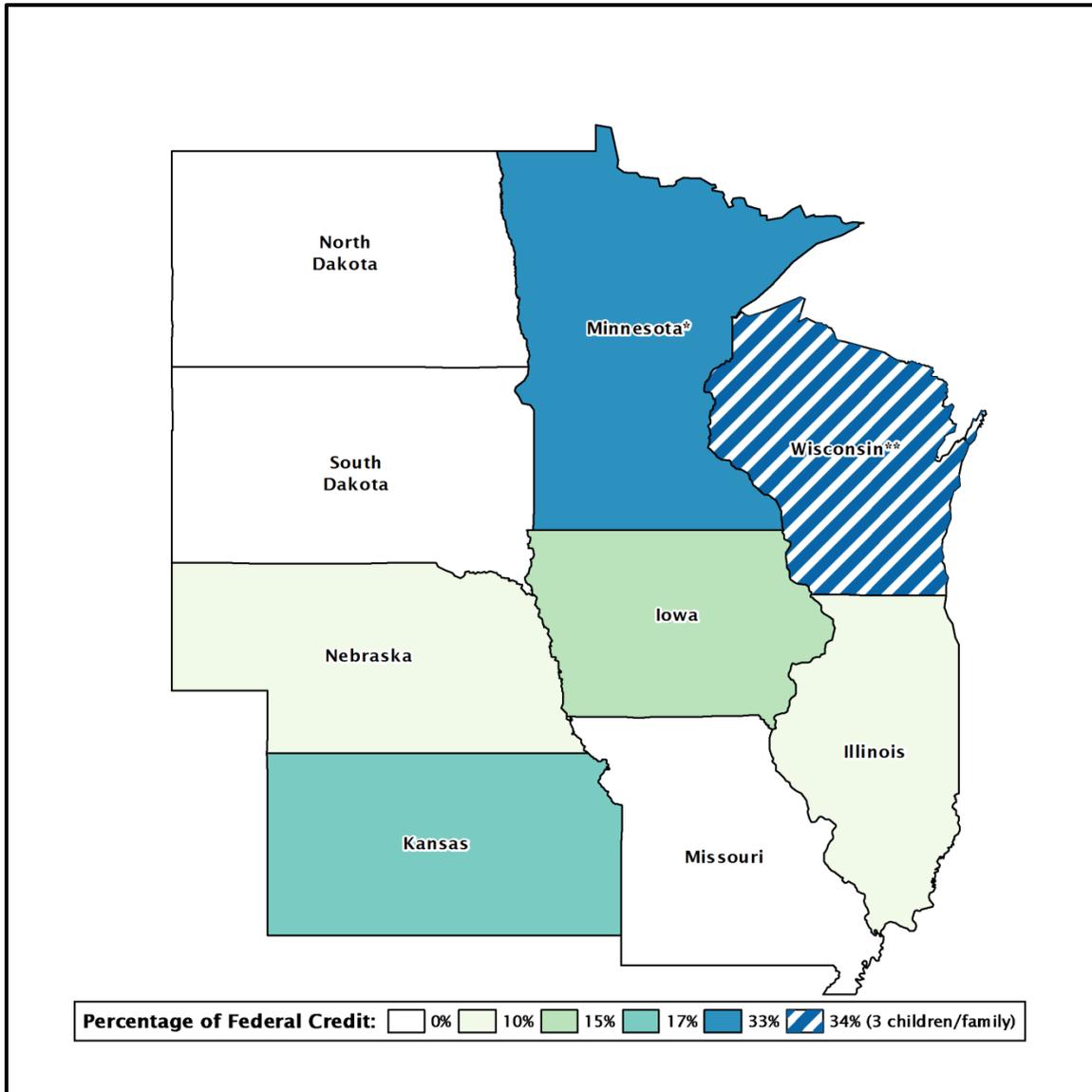


**Source:** National Conference of State Legislatures (NCSL).

**Note:** Minnesota has a minimum wage of \$8.00 per hour effective August 2014 that will continue to rise incrementally until reaching \$9.50 in August 2016. Missouri’s minimum wage is adjusted annually for inflation and will be \$7.65 on January 1, 2015.

Additionally, some surrounding states have enacted a state EITCs. **Map 2**, on the following page, shows these states as a percent match of the federal EITC that each state provides.

**Map 2. State Earned Income Tax Credit in Surrounding States as a Percent Match of the Federal Credit**



**Source:** U.S. Internal Revenue Service.<sup>7</sup>

**Note:** Minnesota has a “Working Family Credit” that is similar to the EITC and averages 33.0% of the federal credit. In Wisconsin, the percentage of the EITC is based on the number of dependents a tax filer has (0.0% credit for zero children; 4.0% credit for one child; 11.0% credit for two children; and 34.0% credit for three children). South Dakota does not have an individual income tax.

The majority of surrounding states are at the federal minimum wage level. Minnesota has both the eventual highest minimum wage, and the highest Working Family Tax Credit (EITC equivalent), when compared to the federal credit.

<sup>7</sup> Internal Revenue Service. States and Local Governments with Earned Income Tax Credits, available at <http://www.irs.gov/Individuals/States-and-Local-Governments-with-Earned-Income-Tax-Credit>

**SUMMARY**

The literature from academic research and economic policy groups on the effects of the minimum wage is vast and represents one of the most studied issues in labor economics. The high volume of papers published has not settled on any precise causal relationship between minimum wage changes and other economic outcomes.<sup>8</sup> Arguments for increasing the minimum wage include increased earnings, increases of aggregate demand, reduced inequality, and reduction in employee turnover. Arguments against increasing the minimum wage include reductions in employment, inability to reduce poverty, increased prices, and reduced profits.

In general terms, addressing income through the minimum wage transfers the cost to employers (business), while addressing income through the EITC transfers the cost to the State (in the form of reduced tax revenues and tax credit expenditures) and targets assistance to a person or family that has children. It should be noted that the minimum wage and the EITC are complementary to the total earnings of the family. As demonstrated earlier, the purchasing power of a static minimum wage is diminished annually by inflation, whereas the benefits of supplemental programs and tax credits are adjusted annually.

In February 2014, the nonpartisan [Congressional Budget Office](#) (CBO) released “The Effects of a Minimum-Wage Increase on Employment and Family Income.”<sup>9</sup> In the report, the CBO examined raising the federal minimum wage to \$10.10 per hour over three years and adjusting annually for inflation as well as raising the federal minimum wage to \$9.00 per hour over two years and not adjusting for inflation afterwards. The report concluded that increasing the minimum wage to \$10.10 per hour will have two principal effects on low-wage workers. Most of them will receive higher pay that increases their family income, and some of those families will see their income rise above the federal poverty threshold. But some jobs for low-wage workers will likely be eliminated and the income of most workers that become jobless will decrease substantially. The share of low-wage workers employed will likely decrease slightly. Under the most likely CBO projections, the income of 900,000 people nationally will rise above the FPG, but total employment may decrease by an estimated 500,000 workers (-0.3%).

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<sup>8</sup> See **Attachment A**. Congressional Research Service. “The Federal Minimum Wage: In Brief,” (May 30, 2013), R43089.

<sup>9</sup> Congressional Budget Office. “The Effects of a Minimum-Wage Increase on Employment and Family Income,” (February 2014), available at <http://www.cbo.gov/publication/44995>



# The Federal Minimum Wage: In Brief

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## Summary

The Fair Labor Standards Act (FLSA), enacted in 1938, is the federal legislation that establishes the minimum hourly wage that must be paid to all covered workers. The minimum wage provisions of the FLSA have been amended numerous times since 1938, typically for the purpose of expanding coverage or raising the wage rate. Since its establishment, the minimum wage rate has been raised 22 separate times. The most recent change was enacted in 2007 (P.L. 110-28), which increased the minimum wage to its current level of \$7.25 per hour.

In addition to setting the federal minimum wage rate, the FLSA provides for several exemptions and subminimum wage categories for certain classes of workers and types of work. Even with these exemptions, the FLSA minimum wage provisions still cover the vast majority of the workforce. Despite this broad coverage, however, the minimum wage directly affects a relatively small portion of the workforce. Currently, there are approximately 3.6 million workers, or 4.7% of all hourly paid workers, whose wages are at or below the federal minimum wage of \$7.25 per hour. Approximately three-quarters of minimum wage workers are age 20 or older and nearly two-thirds work part time.

Proponents of increasing the federal minimum wage argue that it may increase earnings for lower income workers, lead to reduced turnover, and increase aggregate demand by providing greater purchasing power for workers receiving a pay increase. Opponents of increasing the federal minimum wage argue that it may result in reduced employment or reduced hours, lead to a general price increase, and reduce profits of firms paying a higher minimum wage.

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## The Federal Minimum Wage

The Fair Labor Standards Act (FLSA), enacted in 1938, is the federal legislation that establishes the general minimum wage that must be paid to all covered workers.<sup>1</sup> A full discussion of the coverage of the minimum wage is beyond the scope of this report, which provides only a broad overview of the topic. In general, the FLSA mandates broad general minimum wage coverage. It also specifies certain categories of workers who are not covered by FLSA wage standards, such as workers with disabilities or certain youth workers. The act was enacted because its provisions were meant to both protect workers and stimulate the economy. The FLSA also created the Wage and Hour Division (WHD), within the Department of Labor (DOL), to administer and enforce the act.

In 1938, the FLSA established a minimum wage of \$0.25 per hour. The minimum wage provisions of the FLSA have been amended numerous times since then, typically for the purpose of expanding coverage or raising the wage rate. Since its establishment, the minimum wage rate has been raised 22 separate times. The most recent change was enacted in 2007 (P.L. 110-28), which increased the minimum wage from \$5.15 per hour to its current rate of \$7.25 per hour in three steps. For employees working in states with a minimum wage different from that of the federal minimum wage, the employee is entitled to the higher wage of the two.

## FLSA Minimum Wage Coverage

The FLSA extends minimum wage coverage to individuals under two types of coverage—“enterprise coverage” and “individual coverage.”<sup>2</sup> An individual is covered if they meet the criteria for either category. Around 130 million workers, or 84% of the labor force, are covered by the FLSA.<sup>3</sup>

### Enterprise Coverage

The first category of coverage is at the business or enterprise level. To be covered, an enterprise must have at least two employees and must have annual sales or “business done” of at least \$500,000. Annual sales or business done includes all business activities that can be measured in dollars. Thus, for example, retailers are covered by the FLSA if their annual sales are at least \$500,000.<sup>4</sup> In non-sales cases, such as enterprises engaged in leasing property, gross amounts paid by tenants for property rental will be considered “business done” for purposes of determining enterprise coverage.

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<sup>1</sup> In addition, the FLSA provides for overtime pay and child labor protections. The scope of this report is only on the minimum wage provisions. For a broader overview of the FLSA, see CRS Report R42713, *The Fair Labor Standards Act (FLSA): An Overview*, by Gerald Mayer, Benjamin Collins, and David H. Bradley.

<sup>2</sup> 29 U.S.C. §206(a).

<sup>3</sup> U.S. Department of Labor, Wage and Hour Division, *Coverage Under the Fair Labor Standards Act (FLSA)*, Fact Sheet #14, Washington, DC, July 2009, <http://www.dol.gov/whd/regs/compliance/whdfs14.pdf>. Because some individuals are exempt from the minimum wage provisions of the FLSA, the number of workers covered by the minimum wage provisions is presumably lower.

<sup>4</sup> The \$500,000 threshold refers to the annual gross volume of sales. It is not a measure of net revenue or profits.

In addition, regardless of the dollar volume of business, the FLSA applies to hospitals or other institutions primarily providing medical or nursing care for residents; schools (preschool through institutions of higher education); and federal, state, and local governments.

## **Individual Coverage**

The second category of coverage is at the individual level. Although an enterprise may not be subject to minimum wage requirements if it has less than \$500,000 in annual sales or business done, employees of the enterprise may be covered if they are individually engaged in interstate commerce or in the production of goods for interstate commerce. The definition of interstate commerce is fairly broad. To be engaged in “interstate commerce,” employees must produce goods (or have indirect input to the production of those goods) that will be shipped out of the state of production, travel to other states for work, make phone calls or send emails to persons in other states, handle records that are involved in interstate transactions, or provide services to buildings (e.g., janitorial work) in which goods are produced for shipment outside of the state.<sup>5</sup>

## **Exemptions and Subminimum Wages**

The FLSA covers most, but not all, private and public sector employees.<sup>6</sup> Certain employers and employees are exempt from all or parts of the FLSA minimum wage provisions, either through the individual or enterprise coverage or through specific exemptions included in the act. In addition, the FLSA provides for the payment of subminimum wages (i.e., less than the statutory rate of \$7.25 per hour) for certain classes of workers.

## **Excluded from FLSA Minimum Wage Coverage**

The FLSA statutorily exempts various workers from FLSA minimum wage coverage. Some of the exemptions are for a class of workers (e.g., executive, administrative, and professional employees), while others are more narrowly targeted to workers performing specific tasks (e.g., workers employed on a casual basis to provide babysitting services).

The list below is not exhaustive but is intended to provide examples of workers who are not covered by the minimum wage requirements of the FLSA:<sup>7</sup>

- bona fide executive, administrative, and professional employees;<sup>8</sup>

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<sup>5</sup> U.S. Department of Labor, *Coverage Under the Fair Labor Standards Act*, available at <http://www.dol.gov/whd/regs/compliance/whdfs14.pdf>. (Hereafter cited as DOL, *Coverage Under the Fair Labor Standards Act*.) These examples are not exhaustive but are meant to illustrate the relatively broad range of activities comprising “interstate commerce.”

<sup>6</sup> According to the WHD, “more than 130 million workers” are covered by the FLSA. Out of a total civilian labor force of about 155 million, this implies that about 84% of the workforce is covered.

<sup>7</sup> Most exemptions for individuals are in 29 U.S.C. §203(e), 29 U.S.C. §213(a), and 29 U.S.C. §213(d). The list here should not be considered exhaustive as there are various job duties, earnings, and employer characteristic requirements that further define the general exemptions listed here.

<sup>8</sup> The term “bona fide” indicates that job titles alone do not determine exempt status. Rather, employees falling under this exemption must meet criteria related to job duties and pay. See U.S. Department of Labor, Wage and Hour Division, *Exemption for Executive, Administrative, Professional, Computer & Outside Sales Employees Under the Fair Labor Standards Act (FLSA)*, Fact Sheet #17A, Washington, DC, July 2008, [http://www.dol.gov/whd/regs/compliance/fairpay/fs17a\\_overview.pdf](http://www.dol.gov/whd/regs/compliance/fairpay/fs17a_overview.pdf).

- individuals employed by certain establishments operating only part of the year (e.g., seasonal amusement parks, organized summer camps);
- individuals who are elected to state or local government offices and members of their staffs, policymaking appointees of elected officeholders of state or local governments, and employees of legislative bodies of state or local governments;
- employees who are immediate family members of an employer engaged in agriculture;
- individuals who volunteer their services to a private, nonprofit food bank and who receive groceries from the food bank;
- agricultural workers meeting certain hours and job duties requirements;
- individuals employed in the publication of small circulation newspapers;
- domestic service workers employed on a casual basis to provide babysitting;
- individuals employed to deliver newspapers; and
- certain employees in computer-related occupations.

### **Subminimum Wages**

The FLSA also allows the payment of subminimum wages for certain classes of workers, including the following:

- **Youth.**<sup>9</sup> Employers may pay a minimum wage of \$4.25 per hour to individuals under the age of 20 for the first 90 days of employment.
- **Learners.**<sup>10</sup> Employers may apply for special certificates from the Wage and Hour Division of DOL that allow them to pay students who are receiving instruction in an accredited school and are employed part-time as part of a vocational training program a wage at least 75% of the federal minimum wage (\$5.44 at the current minimum wage).
- **Full-Time Students.**<sup>11</sup> Employers may apply for special certificates from the Wage and Hour Division of DOL that allow them to pay full-time students who are employed in retail or service establishments, an agricultural occupation, or an institution of higher education a wage at least 85% of the federal minimum wage (\$6.16 at the current minimum wage).
- **Individuals with Disabilities.**<sup>12</sup> Employers may apply for special certificates from the Wage and Hour Division of DOL that allow them to pay wages lower than the otherwise applicable federal minimum to persons “whose earning or productive capacity is impaired by age, physical or mental deficiency, or injury.” As elaborated in regulations, disabilities that may affect productive capacity include, but are not limited to, blindness, mental illness, mental retardation,

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<sup>9</sup> 29 U.S.C. §206(g).

<sup>10</sup> 29 U.S.C. §214(a).

<sup>11</sup> 29 U.S.C. §214(b).

<sup>12</sup> 29 U.S.C. §214(c).

cerebral palsy, alcoholism, and drug addiction. There is no statutory minimum wage required under this provision of the FLSA, but pay is to be broadly commensurate with pay to comparable non-disabled workers and related to the individual's productivity.<sup>13</sup>

- **Tipped Workers.**<sup>14</sup> Under Section 203(m) of the FLSA, a “tipped employee”—a worker who “customarily and regularly receives more than \$30 a month in tips”—may have his or her cash wage from an employer reduced to \$2.13 per hour, as long as the combination of tips and cash wage from the employer equals the federal minimum wage. An employer may count against his or her liability for the required payment of the full federal minimum wage the amount an employee earns in tips. The value of tips that an employer may count against their payment of the full minimum wage is known as the “tip credit.” Under the current federal minimum wage and the current required minimum employer cash wage, the maximum tip credit is \$5.12 per hour (i.e., \$7.25 minus \$2.13). Thus, all workers covered under the tip credit provision of the FLSA are guaranteed the federal minimum wage.

## Characteristics of Minimum Wage Workers

The most recent data available indicate that there are approximately 3.6 million workers, or 4.7% of all hourly paid workers, whose wages are at or below the federal minimum wage of \$7.25 per hour. Of these 3.6 million workers, approximately 1.6 million earn the federal minimum wage of \$7.25 per hour and the other 2 million earn below the federal minimum wage. As the Bureau of Labor Statistics (BLS) notes, the large number of individuals earning less than the statutory minimum wage does not necessarily indicate violations of the FLSA but may reflect exemptions or misreporting.<sup>15</sup>

Of the estimated 3.6 million workers earning at or below the minimum wage,

- about a quarter (24.1%) are teenagers (ages 16-19),
- nearly two-thirds (64.4%) are female,
- just over one-third (36%) are full-time workers (35 or more hours per week),
- more than 40% work in “food preparation and serving related occupations,”
- just over 15% work in “sales and related occupations,” and

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<sup>13</sup> For details on the process for determining wages under Section 14(c), see U.S. Department of Labor, Wage and Hour Division, *Prevailing Wages and Commensurate Wages under Section 14(c) of the Fair Labor Standards Act (FLSA)*, Fact Sheet #39B, Washington, DC, May 2009, <http://www.dol.gov/whd/regs/compliance/whdfs39b.pdf>.

<sup>14</sup> 29 U.S.C. §203(m).

<sup>15</sup> Bureau of Labor Statistics (BLS), U.S. Department of Labor, *Characteristics of Minimum Wage Workers: 2012*, Washington, DC, February 26, 2013, <http://www.bls.gov/cps/minwage2012.pdf>. BLS produces an annual report on minimum wage workers using data from the Current Population Survey (CPS), which is a monthly household survey used to collect economic and demographic information on the population. The CPS does not ask respondents directly if they earn the minimum wage. Rather the estimate of workers at or below the federal minimum wage is derived from reported earnings on a person's sole (or principal) job. As BLS notes, because the estimates are based on workers paid at hourly rates, with salaried and non-hourly workers excluded, “the actual number of workers with earnings at or below the prevailing minimum wage is undoubtedly understated.”

- nearly three-quarters (72.2%) have at least a high school degree; overall, 8.0% have a bachelor's degree or higher.

## **State Minimum Wages**

States may also choose to set labor standards that are different from federal statutes. The FLSA establishes that if states enact minimum wage, overtime, or child labor laws more protective of employees than those provided in the FLSA, the state law applies. In the case of minimum wages, this means that if an individual is covered by the FLSA in a state with a higher state minimum wage, the individual is entitled to receive the higher state minimum wage. On the other hand, some states have set minimum wages lower than the FLSA minimum. In those cases, an FLSA-covered worker would receive the FLSA minimum wage and not the lower state minimum wage.

Currently, 19 states and the District of Columbia have minimum wage rates above the federal rate of \$7.25 per hour. These rates range from \$7.35 per hour in Missouri to \$9.19 in Washington state. Four states have minimum wage rates below the federal rate and five have no minimum wage requirement.<sup>16</sup> In the states with no minimum wage requirements or wages lower than the federal minimum wage, only individuals who are not covered by the FLSA are subject to those lower rates.

## **Arguments For and Against Raising the Minimum Wage**

The literature on the effects of the minimum wage is vast and represents one of the more well-studied issues in labor economics. As such, this topic has resulted in hundreds of academic and non-academic publications. It is beyond the scope of this section to summarize or synthesize this literature. Broadly speaking, there is not universal consensus on the causal relationship between changes in minimum wage and other economic outcomes. This section presents a brief summary of the primary arguments that proponents and opponents make regarding minimum wage increases.

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<sup>16</sup> U.S. Department of Labor, Wage and Hour Division, *Minimum Wage Laws in the States*, <http://www.dol.gov/whd/minwage/america.htm>.

## **Arguments For Increasing the Minimum Wage<sup>17</sup>**

### **Increases Earnings**

Proponents of an increase in the minimum wage often assert that raising wages can be a component in reducing poverty for individuals and families and a direct way to increase earnings for lower-income workers. Assuming the minimum wage earner does not suffer a loss of employment, hours, or other wage supplements as a result of the increase, then an increased minimum wage should close the gap between earnings and the poverty line. For example, a single parent with two children who works full-time, year-round at the current minimum wage has earnings of about 76% of the poverty line. An increase in the minimum wage to \$9 per hour would raise that family's earnings to about 94% of the poverty line.<sup>18</sup>

### **Increases Aggregate Demand**

Proponents of minimum wage increases also argue that additional income for individuals will result in increased aggregate demand in the economy. Adult minimum wage households have a higher marginal propensity to spend additional income than higher-income households. Therefore, to the extent that minimum wage increases raise the income of adult minimum wage households, a minimum wage increase could have a stimulative effect on the economy.

### **Reduces Inequality**

Proponents of an increase in the minimum wage argue that it could help reduce earnings inequality by setting a higher floor at the lower end of the wage scale. At the level of an individual business, wage compression might occur if the minimum wage increases at the low end of the pay scale were offset by freezes or reductions in pay at higher levels of pay. That is, the spread between the lowest earners and the highest earners at a business might narrow if the business adjusted to higher pay for minimum wage earners by keeping flat or reducing pay for higher earners. Economy-wide, the size of the gap between low-wage earners and middle and high earners might decrease depending on how widely wage compression was used as a channel of adjustment to minimum wage increases.

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<sup>17</sup> For examples of arguments in favor of increasing the federal minimum wage, see David Cooper and Doug Hall, *Raising the Federal Minimum Wage to \$10.10 Would Give Working Families, and the Overall Economy, A Much-Needed Boost*, Economic Policy Institute, Briefing Paper #357, Washington, DC, March 13, 2013, <http://www.epi.org/files/2013/bp357—federal-minimum-wage-increase.pdf> and Christian E. Weller and Nick Bunker, *A Higher Minimum Wage Will Not Hurt U.S. Businesses*, Center for American Progress, Washington, DC, February 15, 2013, <http://www.americanprogress.org/issues/economy/news/2013/02/15/53603/a-higher-minimum-wage-will-not-hurt-u-s-businesses/>.

<sup>18</sup> These figures, produced by CRS, are based on estimated 2014 poverty thresholds. For a family of three the poverty threshold is \$19,820. At the current minimum wage of \$7.25 per hour, a full-time, year-round worker would earn \$15,080, or 76% of this threshold. At a minimum wage of \$9.00 per hour, a full-time, year-round worker would earn \$18,720, or 94% of this threshold.

## **Reduces Employee Turnover**

A higher wage may lead workers to choose to stay in their jobs longer than they otherwise would have under a lower wage. Because high turnover is costly to businesses, proponents of minimum wage increases argue that an increase in the minimum wage may be offset by lower turnover costs.

## **Arguments Against Increasing the Minimum Wage<sup>19</sup>**

### **Reduces Employment**

Much of the popular discussion about the effects of a minimum wage increase focuses only on one channel of adjustment—employment. In particular, opponents of a minimum wage or of minimum wage increases assert that increases in the minimum wage will result in increased unemployment, either broadly or for particular subpopulations of the labor market (e.g., youth, less skilled or experienced workers), or a reduction in hours worked. In a standard competitive model of the labor market, the introduction of or increase in the minimum wage (a price increase) results in employment losses (demand decrease).

### **Does Not Reduce Poverty**

Because the minimum wage is not targeted to workers in low-income households, it is possible that the minimum wage does not reduce poverty to the extent a targeted policy might (e.g., tax credit). The minimum wage is a relatively blunt anti-poverty policy as it may raise wages for people not in poverty such as suburban teenagers who live in a middle- or high-income household.

### **Increases Prices**

Another way minimum wage increases might be absorbed is through changes in prices. Specifically, employers facing a higher mandated minimum wage might choose, if possible, to pass on the extra costs of labor to the consumers through higher prices. If minimum wage increases result in an increase in the aggregate price level, then the inflationary effects would erode some of the purchasing power of both those receiving raises and everyone else in the economy.

### **Reduces Profits**

A decrease in profits could be another means of adjustment to an increase in the minimum wage. The ability of any given business to lower profits to pay for mandated increases depends on the profit margins of that firm.

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<sup>19</sup> For examples of arguments against increasing the federal minimum wage, see Mark Wilson, *The Negative Effects of Minimum Wage Laws*, Cato Institute, Washington, DC, September 2012, <http://www.downsizinggovernment.org/sites/downsizinggovernment.org/files/pdf/negative-effects-minimum-wage-laws.pdf> and James Sherk, *Who Earns the Minimum Wage? Suburban Teenagers, Not Single Parents*, The Heritage Foundation, Issue Brief No. 3866, Washington, DC, March 1, 2013, [http://thf\\_media.s3.amazonaws.com/2013/pdf/ib3866.pdf](http://thf_media.s3.amazonaws.com/2013/pdf/ib3866.pdf).

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