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IWS Issue Brief - Wages to Live By...Or Not

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Abstract
[Excerpt] There is no single or simple solution to the poverty and income inequality quagmire. Effecting policy change at the national level would require the type of macroeconomic strategies that are likely to engender fierce opposition and stonewalling tactics. And yet, criticism of the economic status quo, in which capital begets more capital and wage earners struggle to become, or remain, middle class, is growing louder. Some politicians are beginning to take notice and socio-economic policies may yet be devised to mitigate the worst of the excesses. In the meantime, progressive activists see more opportunity to make a difference at the local level, where the living wage movement is indeed making strides. Linking the cause with other hot-button issues that play out locally, including the renewal of American cities large and small, economic development and new jobs, privatization of government services, and grassroots empowerment, enables proponents to rally support for the living wage agenda. Whether the living wage movement eventually becomes a national force that seriously dents our poverty statistics remains an open question.

Wages to Live By…Or Not

Big news this past July: The federal minimum wage jumped 70 cents to $5.85 an hour – a full ten years after the last increase. Next summer the wage floor will rise again, to $6.55, and in 2009 it will top out at $7.25. At this higher level, individuals working 40-hour weeks and taking no unpaid time off will earn $15,080 a year.

Could you live on that? I couldn't. What if you're supporting a spouse and two children? The federal poverty "guideline" last year for a family of four was $20,650, which qualified you for assistance programs such as Head Start, food stamps, and health insurance for the kids. If it's cash assistance you're after, such as Temporary Assistance for Needy Families, eligibility is determined by a different set of standards. Then there is the earned income tax credit (EITC), which provides financial aid in the form of a refund or credit on your taxes. Worth up to $4,536 for the 2006 tax year if your earned income was less than $36,348 ($38,348 if you file jointly with your spouse) and you had at least two dependent children (lesser amounts are paid if you don't), the EITC is currently claimed by some 22 million families a year.

A Living Wage

Still having trouble making ends meet? Then consider joining the forces advocating for a "living wage." By living wage, its proponents generally mean hourly pay sufficient to sustain a minimally modest standard of living, absent any government subsidies, for a family with two children. This wage target is admittedly subjective, one that has more to do with social and moral imperatives than with market mechanisms that are usually understood to mediate the supply of, and demand for, labor. But it is a conception that has attracted a great deal of attention since its debut in Baltimore in 1994. A stagnant minimum wage with continuously diminishing purchasing power, mounting income inequality, deteriorating job options for low-wage/low-skilled workers, new welfare rules with time limits on assistance, and generalized concern about the pace and direction of local economic development have jointly fueled the living wage movement. The opposition, meanwhile, has been energized by assertions that such an artificially determined wage floor hurts the people it is intended to benefit, advances the self-serving interests of public sector unions, and creates more unnecessary regulation.

Today, some 140 municipalities (cities and counties) and the state of Maryland have passed legislation mandating a living wage for certain classes of workers. (Several states, including Missouri, Colorado, Arizona, and Louisiana have taken steps to pre-empt the ability of local governments to pass living wage laws.) Details of the ordinances vary, but wages are typically set at $9-11 an hour; some incorporate annual increases and some tack on an extra $1.50 or so if health and/or vacation benefits are not included. Communities with a particularly high cost of living may require even higher pay: Sonoma, CA, for example, where the cost of living is 139% of the national average, fixes the living wage at $13.20 if there is no health plan and $11.70 if there is; the Santa Fe, NM ordinance pegged the living wage at $9.50 an hour for 2006-2007 and calls for annual increases beginning in 2009 to keep pace with the consumer price index for urban wage earners in the western region – this in a city where the cost of living is 18% higher than the national average and average earnings per job are 23% below.

Workers affected by living wage legislation tend to fall into one of several categories based on their place of employment. Some ordinances are aimed at employers who have service contracts with, or who receive tax subsidies, loans, or other business assistance from, the local government. Others target employers who hold a lease, concession, or franchise granted by the local government or a subcontract from an employer who falls into one of these other categories. In rare instances, employers with more than some specified number of workers on the payroll are obligated to pay the living wage. Local ordinances may also encompass more than one group of employers. The degree to which these laws impact the wages of affected workers seems to depend in large part on the community's commitment to implementation: some ordinances have strong administrative structures and/or enforcement powers while others are lax in one or both dimensions.

For and Against

Living wage proponents constitute a broad coalition of neighborhood, religious, and labor groups. The motivations underlying their activism in support of the living wage range from the obvious socio-economic and moral justice concerns about families living on $15,000 a year to political and equity objections to taxpayer subsidies of low-wage employers. Living wage proponents argue that employers who benefit from government largesse – be it a contract for services rendered, the advancement of economic development goals through tax abatements, loans, grants, and the like, or any other form of beneficial business dealings with the government – should not be allowed to double-dip into the public till. That is, these employers should at least pay wages that enable their workers to live a life that does not necessitate taxpayer-supported handouts passed through the government. Some in the movement also foresee a welcome ripple effect of rising wages for workers holding similar positions at workplaces not covered by the legislation and jobs at levels just above those getting bumped up to the higher living wage. They further acknowledge that a living wage law might dissuade government agencies from contracting out, or privatizing, public services because the higher pay scale imposed on bidders might not generate any cost savings. And finally, living wage campaigns often facilitate the formation of progressive coalitions of concerned citizens and other actors in civil society that might then influence economic and other key government policies.

Opposition to the living wage concept is rooted in a more conservative view of the public's role in policymaking and the functioning of labor markets. In fact, critiques of the living wage echo many of the arguments long advanced against the minimum wage. Detractors assert that artificial wage floors negatively affect low-wage, low-skill workers by inducing employers to reduce demand for the labor supplied by these workers. In other words, higher wages discourage hiring, particularly of the most vulnerable populations (minority youth and high-school dropouts). Critics also warn that above-market wage floors for contract services will deter bidding on these contracts and, where an ordinance aims at employers receiving "business assistance," will dampen local investment and thwart economic development. They further contend that the living wage is an inefficient policy tool because it affects only some employers and a small number of workers in just a few concentrated geographic regions. Moreover – and more importantly – its aim is scattershot. Being poor is not necessarily synonymous with earning a minimum, or even a living, wage. Poor people may be paid higher wages but just not work enough hours, while many non-poor individuals, such as teenagers from middle-class families, who earn the minimum do not "need" higher pay. So, the reasoning goes, low-wage workers would be better served by strategies that aim to improve their skills and augment the number of hours on the job.

The sparseness of data available to analyze the living wage experiments complicates the ability of either side of the debate to make its case. Spotty data reflects the relative newness of the ordinances, the small sample size, the wide variety of the laws' specifications, and the diverse contexts in which they operate (e.g., local economic conditions and the political climate). Even with the limited data at hand, there is no agreement among researchers or activists on which type of ordinance is most or least effective in boosting workers' pay, and why. Some argue that laws aimed at employers with government contracts are easiest to enforce while others say business assistance measures have the largest impact on workers.

Opponents and proponents alike rely on their preferred studies and ideological foundations to support their respective positions. Much of the relevant research relates to the minimum wage, which has been a feature of the national economy since the Fair Labor Standards Act was adopted in 1938. Critics cite reports noting that family heads earning minimum wage tend to be younger than 30 and that young workers typically experience a sizeable jump in wages within the first year of employment. They also point to findings that show higher wage floors crowd out adult wage earners and other studies that conclude imposed minimums lead to declines in minority employment in general and to more substantial job loss among those with the least skills. Indeed, economic theory suggests that higher labor costs prompt employers to seek out more productive substitutes, such as additional technology and/or higher-skill workers. Some of the living wage-specific research does in fact indicate that employers holding government contracts who are obligated to pay a living wage maximize the efficient use of their resources by reallocating labor: higher skill/higher wage employees who already earn rates at or above the living wage are assigned to the contract work and less skilled/lower wage workers are placed in jobs not affected by the wage floor.

Proponents counter that the added costs associated with a living wage are actually quite minor. They concede that employers will be motivated to offset wage increases with productivity gains, but insist that the improved morale, reduced absenteeism, and decreased turnover that follow upon higher wages compensate for part of the extra cost – an argument that some qualitative studies seem to support. A 2003 survey of 20 cities and counties with living wage ordinances found that the costs associated with the higher wage accounted for less than 1% of the cities' budgets while another study found that bidding on contracts by private-sector vendors was not deterred (Thompson and Chapman). Another report shows that passage of a living wage ordinance by a city, but not by its surrounding suburbs, does not hinder employment growth or disadvantage workers (Buss and Romeo). In Los Angeles, a living wage law passed in 1997 covering service contractors, employers who receive large subsidies from the city, and employers holding concession agreements (notably, at the airport) generated wage increases for more than 10,000 minimum wage workers, the vast majority of whom were adults, worked fulltime and had, at most, a high school degree. The data also indicate that employers made few employment cutbacks despite the jump in wages (Fairris et al).

The Tax Credit

But even a living wage – even one that incorporates health and vacation benefits – just barely lifts a family out of poverty. At $11.50 an hour (at the high end of the living wage scale), a worker putting in 40 hours a week for 52 weeks a year would earn $23,920. For some families, this is just enough to cover the most basic necessities; for others, it is woefully inadequate. Given that existing living wage ordinances affect a limited number of workers and provide only the smallest margin of financial relief, anti-poverty advocates also favor additional policy prescriptions. One that holds great appeal is the earned income tax credit, or EITC.

A stronger, though still imperfect, anti-poverty strategy calls for combining the living wage with the EITC. (A better option would be an even higher federal minimum wage, which would affect all low-wage workers, in concert with the EITC.) The living wage and the EITC each have their pros and cons as policy tools. For example, higher wages reach people in each paycheck while the tax credit arrives once a year in a lump sum. (Recipients may choose to collect their credit piecemeal in each paycheck, though few opt to do so.) The living wage helps those whose hourly pay was below the new floor but does nothing for those who earn higher wages in part-time jobs. The tax credit mostly helps the working poor who have dependent children but provides little relief to singles or couples without children, or to workers too old or too young to qualify. The living wage reaches only a select few while the EITC is available to millions of low-income workers. Neither, however, does anything for poor individuals who don't work at all.

On its own, the EITC attracts broad support despite equivocal research findings regarding its impact. Since the EITC was introduced in 1975, partly as a work incentive and partly to help low-income families offset regressive payroll taxes, it has been expanded several times. In addition, 20 states and the District of Columbia now offer their own EITC to augment the federal program. The structure of the EITC increasingly rewards work through ever larger tax credits up to a certain level of income, then hits a plateau where the tax credit remains fixed until another income ceiling is reached, after which the tax credits begin to phase out until a final maximum income level. To qualify, recipients must have dependent children and fall between the ages of 25 and 64.

During the 2003 tax year, the EITC paid out $39 billion, with the bulk of the benefits going to families earning $10,000-$20,000. Studies indicate the EITC – especially in concert with a state EITC – has helped reduce poverty, most notably among children. Its future impact is a bit uncertain, however, given the recent increase in the federal minimum wage and the lack of any pronounced intention by Congress to raise income ceilings and credit allowances beyond adjustments for inflation. Still, research shows that the EITC decreases reliance on public assistance and also serves as a form of wage insurance for families temporarily experiencing job loss. And while it has been particularly effective in inducing single mothers to enter the labor force, the labor supply effects for other less-skilled workers is mixed. Some research suggests the EITC encourages increased labor force participation but others find it discourages people from working longer hours.

Like the living wage, the EITC has its weaknesses. For one, the vast majority of households with incomes below the poverty guideline do not qualify for the credit because of age restrictions, the absence of dependent children, or a lack of reportable earnings. Moreover, the Internal Revenue Service estimates that up to 25% of eligible taxpayers do not collect any benefits at all because they fail to file the necessary paperwork; some critics charge this reflects inadequate outreach to needy populations. Others assail the concept of an EITC, calling it a form of welfare or decrying a formula that they contend discourages work and marriage. Progressive critics allege it is yet another taxpayer-supported program that enables employers to externalize their labor costs (i.e., pay low wages knowing workers will get a boost from the tax credit). And yet, the EITC maintains bipartisan support in Congress and backing from anti-poverty advocates. Living wage proponents likewise attest to its overall value even though its impact is muted for workers who are paid those higher living wages.

A Final Word

There is no single or simple solution to the poverty and income inequality quagmire. Effecting policy change at the national level would require the type of macroeconomic strategies that are likely to engender fierce opposition and stonewalling tactics. And yet, criticism of the economic status quo, in which capital begets more capital and wage earners struggle to become, or remain, middle class, is growing louder. Some politicians are beginning to take notice and socio-economic policies may yet be devised to mitigate the worst of the excesses. In the meantime, progressive activists see more opportunity to make a difference at the local level, where the living wage movement is indeed making strides. Linking the cause with other hot-button issues that play out locally, including the renewal of American cities large and small, economic development and new jobs, privatization of government services, and grassroots empowerment, enables proponents to rally support for the living wage agenda. Whether the living wage movement eventually becomes a national force that seriously dents our poverty statistics remains an open question.

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