



**CONGRESSIONAL BUDGET OFFICE  
PRIVATE-SECTOR MANDATE STATEMENT**

May 9, 2001

**S. 277  
Fair Minimum Wage Act of 2001**

*As introduced on February 7, 2001*

**SUMMARY**

S. 277 would amend the Fair Labor Standards Act of 1938 (FLSA) to increase the federal minimum wage rate in three steps from \$5.15 per hour today to \$6.65 per hour beginning on January 1, 2003. It would also apply the minimum wage provisions of the FLSA to the Commonwealth of the Northern Mariana Islands (CNMI).

**PRIVATE-SECTOR MANDATES CONTAINED IN BILL**

S. 277 would impose a mandate on private-sector employers covered by the FLSA because it would require them to pay a higher minimum wage rate than they are required to pay under current law.

**ESTIMATED DIRECT COST TO THE PRIVATE SECTOR**

CBO's estimate of the direct cost of the private-sector mandates in S. 277 is displayed in the following table. The cost would exceed the threshold specified in the Unfunded Mandates

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Provision	By Fiscal Year, in Billions of Dollars				
	2002	2003	2004	2005	2006
Increase the federal minimum wage	3.8	6.9	7.0	6.2	5.5
Apply the minimum wage to the CNMI	0.1	0.1	0.2	0.2	0.2

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Reform Act of 1995 (\$113 million in 2001, adjusted annually for inflation) in each of the first five years following enactment.

## **BASIS OF ESTIMATE**

S. 277 would increase the federal minimum wage from \$5.15 per hour to \$5.75 per hour beginning 30 days after the date of enactment, to \$6.25 per hour beginning on January 1, 2002, and to \$6.65 per hour beginning on January 1, 2003. In addition, it would apply the minimum wage provisions of the FLSA to the CNMI, with a transition period that would begin 30 days after the date of enactment. It would not change other sections of the FLSA that establish different rules for certain workers and employers, including the provision permitting employers to pay teenagers \$4.25 per hour during the first 90 days of employment. For the purpose of this estimate, CBO assumed that S. 277 would be enacted on September 1, 2001.

To estimate the direct cost to private employers of raising the minimum wage, CBO used information on the number of workers whose wages would be affected in October 2001 and subsequent months, the wage rates these workers would receive in the absence of the bill, and the number of hours for which they would be compensated.

The estimate was made in two steps, which are described in more detail below. First, CBO used data from the Current Population Survey (CPS) to estimate how much it would have cost employers to comply with the mandate had they been required to do so in early 2001. Second, that estimate was used to project the costs to employers beginning in October 2001, taking into account the expected decline over time in the number of workers in the relevant wage range. The methods used for this estimate are similar to those used for CBO's estimates of a similar proposal made in 1999 but are updated to include more recent information.

Relatively little information is available regarding the effect of the minimum wage provisions on the CNMI. The current minimum wage there is \$3.05 per hour. The bill would increase that minimum wage to \$3.55 per hour beginning 30 days after the date of enactment. It would increase it to \$4.05 per hour five months later. Thereafter, the minimum wage in the CNMI would increase by \$0.50 per hour every six months until it became equal to the federal minimum wage. Based on information provided by the Office of Insular Affairs, U.S. Department of the Interior, roughly 30,000 private workers are employed in the CNMI at about \$3.05 per hour, and few are employed at wage rates between \$3.06 and \$6.65 per hour. Once the minimum wage rate in the CNMI reaches \$6.65 per hour, the bill would impose a mandate on private employers of about \$200 million per year, assuming that the wages of 30,000 workers would be affected.

## **Estimates from the Current Population Survey**

Data on hourly wage rates contained in the CPS are the basis for CBO's estimate of the number of private-sector workers nationwide who were paid a wage rate in the relevant range during the first three months of 2001. At that time, about 600,000 workers in the private sector reported being paid exactly \$5.15 per hour. In addition, about 550,000 workers reported being paid \$5.00 per hour; CBO assumes that these workers were also covered by the \$5.15 minimum wage and misreported their wage rate. An additional 8.3 million workers were paid between \$5.16 and \$6.64 per hour.

Roughly one-third of the workers in the relevant wage range were teenagers. Based on information from the Bureau of Labor Statistics, CBO assumes that about 30 percent of those teenagers were in their first 90 days of employment with their current employer and therefore not covered by the increase in the minimum wage required by S. 277.

CBO estimates that if the private-sector workers who were paid between \$5.15 and \$5.74 per hour in early 2001 had been paid \$5.75 instead (with no change in the number of hours worked), their employers would have paid them approximately \$125 million in additional wages each month. If the workers who had been paid between \$5.15 and \$6.24 had been paid \$6.25, their employers would have incurred an additional wage bill of about \$400 million per month. If the workers who had been paid between \$5.15 and \$6.64 had been paid \$6.65, their employers would have incurred an additional wage bill of about \$775 million per month. Moreover, employers would have been required to pay their share of legally mandated costs that are tied to a worker's wages; these payments are included in CBO's estimate of the total direct cost of the mandate.

## **Applying the Estimates from the CPS to the Projection Period**

The monthly cost to employers of the proposed increases in the minimum wage would be smaller in the future than now because the number of workers in the affected range will decline over time even if the minimum wage is not raised. For example, between 1992 and 1995, the number of workers earning \$4.25 per hour (the minimum wage rate during that period) fell by about 30 percent. Between September 1997 and March 2001, the number of workers paid \$5.15 per hour (the minimum wage rate established in September 1997) fell by an even greater amount as market forces and increases in state minimum wage rates raised the level of wages paid. CBO assumes that the direct cost of the mandate would steadily decrease at a rate of about 10 percent per year throughout the projection period because of those effects.

Estimates for each fiscal year were made by aggregating the monthly costs. The estimate for fiscal year 2002 would include the cost of a \$5.75 minimum wage for three months and a \$6.25 minimum wage for nine months. The estimate for 2003 would include the cost of a \$6.25 minimum wage for three months and a \$6.65 minimum wage for nine months. The estimate of the direct cost to the private sector is highest for 2004, when all twelve months would be at \$6.65 per hour.

## **Limitations**

Estimates of the direct cost of this mandate are uncertain for at least two important reasons. First, the main source of data—the CPS—is subject to sampling error and other problems when used for this purpose. For example, there is uncertainty about the actual wage rate of workers who said that they were paid \$5.00 per hour. CBO assumed that those workers were actually paid the federal minimum wage rate of \$5.15 because there is no evidence that compliance with the Fair Labor Standards Act fell. In addition, the wage rates of certain other low-wage workers (some who reported being paid below \$5.00 per hour and some who were not paid on an hourly basis) would also be affected by an increase in the statutory minimum, but the CPS does not provide reliable estimates of the number of such workers or of the increase in mandate costs that would be attributable to them.

A second source of uncertainty in this estimate is the fact that there is no solid basis for projecting the future number of workers who will have wage rates in the relevant range, their precise wage rates, or the number of hours they will work under current law. The annual decline estimated from earlier periods could turn out to be too rapid or too slow.

## **INDIRECT EFFECTS OF AN INCREASE IN THE MINIMUM WAGE**

An increase in the minimum wage rate from \$5.15 to \$6.65 would require employers to raise the wage rate paid to the lowest-paid workers covered by the FLSA by 29 percent and would require employers to raise the wages of workers in the range between the old and the new statutory rates by smaller amounts. As under current law, employers could still pay teenage workers \$4.25 per hour during their first 90 calendar days of employment.

Economists have devoted considerable energy to the task of estimating how employers would respond to such a mandate. Although most economists would agree that an increase in the minimum wage rate would cause firms to employ fewer low-wage workers, there is considerable disagreement about the magnitude of the reduction. The main reason for this disagreement is that it has proven difficult to distinguish the effects on employment of past

changes in the minimum wage from other changes in the labor market. Moreover, the estimates from such analyses are difficult to apply to future changes because labor market conditions will be different.

Employers could respond to an increase in the federal minimum wage in many different ways. In addition to holding down the effect on their payroll costs by reducing the size of their workforce, they could reduce the number of hours worked by some of their employees. Because many of the workers are on part-time schedules, reducing hours might be easier to do than it would be if all workers were employed on fixed eight-hour schedules.

Other ways that employers might respond to an increase in the federal minimum wage would not involve adjustments in employment levels or hours. For example, some employers might reduce fringe benefits. Some employers might attempt to pass along at least a portion of the additional payroll costs to their customers by raising prices. They might be successful in doing so if their competitors were also faced with higher labor costs because of the increase in the minimum wage.

Based on CBO's review of a number of relevant studies, a plausible range of estimates of the potential job losses associated with an increase in the minimum wage to \$6.65 in January 2003 is roughly 200,000 to 600,000 jobs.<sup>1</sup> But even this wide range does not convey the considerable uncertainty that surrounds any estimate of the impact of raising the minimum wage.

On the one hand, the low end of this range might be more realistic because the number of minimum-wage workers is smaller today than it was during most of the time periods when the employment effects were estimated in the literature. In early 2001, only about 1 million workers were paid the federal minimum wage. During much of the past two decades, when many of the studies were undertaken, between 2 million and 4 million workers were paid the minimum wage. Moreover, the 1996 increase in the minimum wage amended the FLSA to permit employers to pay teenagers \$4.25 per hour for the first 90 days, and the current bill would not change this provision. While few employers are using this option, its availability could cushion employment losses if labor markets weakened.

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<sup>1</sup> See, for example, Alison J. Wellington, "Effects of the Minimum Wage on the Employment Status of Youths: An Update," *Journal of Human Resources*, Vol. XXVI, No. 1 (Winter 1991), pp. 27-46, Charles Brown, "Minimum Wage Laws: Are They Overrated?" *Journal of Economic Perspectives*, Vol. 2, No. 3 (Summer 1988), pp. 133-145, David Card and Alan B. Krueger, *Myth and Measurement: The New Economics of the Minimum Wage* (Princeton University Press, 1995), Marvin H. Koters, editor, *The Effects of the Minimum Wage on Employment* (AEI Press, 1996) and Richard V. Burkhauser, Kenneth A. Couch, and David C. Wittenburg, "Who Minimum Wage Increases Bite: An Analysis Using Monthly Data from the SIPP and the CPS," *Southern Economic Journal*, Vol. 67, No. 1 (July 2000), pp. 16-40.

On the other hand, a 29 percent increase in the federal minimum wage rate would be a larger increase than employers had to adjust to in the recent past. The most recent legislation raising the minimum wage -- from \$4.25 to \$5.15, in two steps -- required a 21 percent increase. Moreover, even though the number of workers paid the minimum wage is relatively small, about 9.5 million workers were paid wages in the affected range (\$5.15 to \$6.64) in early 2001.

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