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Who needs a raise? Potential impact of a higher Ohio minimum wage

Amy Hanauer

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Authors

Amy Hanauer is Executive Director of Policy Matters Ohio. She has a Master's of Public Administration from the University of Wisconsin at Madison and a Bachelor of Arts from Cornell University. Prior to helping found Policy Matters, Amy was a Senior Associate at the Center on Wisconsin Strategy. For Policy Matters, Amy writes the *State of Working Ohio* series and has written about the Earned Income Tax Credit and other issues related to taxes, wages, and workers.

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We are also grateful to Susan Bottino and the staff of Policy Matters Ohio for review of earlier drafts. We take full responsibility for any remaining errors.

As always, we are grateful to the Joyce Foundation, the George Gund Foundation, and the St. Ann Foundation, which support our research or distribution of research on working people. We dedicate this paper to the Ohio workers who earn less than $6.85 an hour, and to their children.

Policy Matters Ohio, the publisher of this study, is a nonprofit, nonpartisan research institute, dedicated to research that matters to working people and their families in Ohio. Policy Matters seeks to broaden the debate about economic policy in Ohio by providing quantitative and qualitative analysis of important issues. Other areas of inquiry for Policy Matters have included unemployment compensation, workforce policy, wage distribution, education, housing and economic development. For downloadable versions of this and other research, see http://www.policymattersohio.org.

Executive Summary

For 68 years the minimum wage has been an important feature of American policy. It is part of the public structure we need for a successful economy that works for all of us—an economy that values work and protects those who play by the rules. In recent years, however, the minimum wage has been allowed to wither.

The federal minimum wage of $5.15 an hour has less purchasing power than at any time in more than fifty years. Since 1968, the value of a minimum wage paycheck has plunged more than thirty percent. A full-time minimum wage worker earns only $10,712 a year, less than two-thirds of the federal 3-person poverty line ($16,600 per year in 2006).

The federal government has not raised the minimum wage since 1997 but twenty states have raised their minimum wages,[1] coalitions are pushing ballot initiatives in seven states, and legislation has been introduced in many others.

Although most Ohio workers have always been protected by the federal minimum wage, Ohio has, until recently, been in the unusual situation of having a minimum wage *below* the federal level. Legislators recently voted to increase the state minimum wage to correspond to the federal level, although it has not yet been signed into law. For the narrow slice of workers not protected by the federal minimum wage, this change could provide some modest relief.

To address the broader problem of the declining value of the minimum wage that applies to most workers, a coalition of labor unions, community organizations and other citizens is seeking to put an initiative on the November 2006 ballot. The measure would raise the Ohio minimum wage to $6.85 an hour by 2007 with annual cost-of-living-adjustments thereafter.

That proposal would raise wages for about 719,000 Ohio workers—14 percent of the state's workforce. Directly affected are 297,000 workers who currently earn less than $6.85. An additional 423,000 are indirectly affected – already earning at least $6.85 but likely to still get a modest wage increase as employers adjust pay scales to accommodate raises for minimum wage employees.

If the wage is increased, those earning under $6.85 prior to the increase will get an average estimated 80 cent raise, and those earning more than $6.85 will get an average estimated 26 cent raise. Other findings include:

♦ About three quarters of those affected (74 percent) are age 20 or older.
♦ Many (28 percent) are married, and about one in five is a parent. Approximately 253,000 Ohio children have a parent who would see a raise under this proposal.
♦ Families with workers who would see a raise rely on those workers for more than half of the families' weekly earnings, on average.

[1] Includes Michigan where the governor will soon sign an increase, and counts Washington, D.C. as a state

♦ In 38 percent of affected families, these workers provide the entire family weekly earnings.
♦ More than half of affected workers (51 percent) come from the bottom forty percent of the household earnings spectrum, living in households with total weekly earnings less than $737. The bottom forty percent of households currently takes in less than 16 percent of worker earnings, but would get more than half of the wage increases resulting from the $6.85 wage level.
♦ The vast majority (78%) work at least 20 hours a week; 43 percent work full time.
♦ Fifty-eight percent are women and 42 percent are men.
♦ Fourteen percent of all white workers and 15 percent of all black workers could expect to see a raise under the proposal.

Restoring the minimum wage to a more adequate level would generate raises for 719,000 Ohio workers and help our state to again value work and workers. The federal government has allowed the minimum wage to erode to its lowest level in more than fifty years. Joining the twenty states (including Washington and Michigan) that have set a higher standard will help put Ohio back on the economic high road.

Introduction

For 68 years the minimum wage has been an important feature of American policy. It is part of the public structure we need for a successful economy that works for all of us—an economy that values work, offers a more level playing field, and better protects those who play by the rules. The minimum wage, however, has been allowed to wither in value and is now lower, in real terms, than at any other point in more than fifty years.

Most Ohio workers have always been covered by the federal minimum wage. For the narrow slice of workers not protected by the federal law, Ohio has, until recently, been in the unusual situation of having a minimum wage *below* the federal level. Ohio legislators recently voted to make the federal wage apply to more Ohio workers, a move that awaited the Governor's signature as of this writing. For the 92,000 Ohio workers paid less than $5.15 an hour, this adjustment could provide some modest relief.

However, because the federal minimum wage is at its lowest real value since 1955, minimum wage workers who are supporting even one other person are currently unable to climb above the official poverty line with full-time, year-round work. The low level of the federal wage and its failure to keep pace with inflation has inspired citizens and legislators in twenty states[2] to raise their minimum wage above the federal level. In about ten other states, coalitions are gathering signatures for minimum wage initiatives or legislation has passed at least one chamber of the state legislature.

In Ohio, a coalition of workers, unions, community organizations and other citizens is seeking to put an initiative on the November 2006 ballot that would raise the Ohio minimum wage to $6.85 an hour by 2007 with annual cost-of-living-adjustments thereafter.

[2] Includes Michigan where the bill awaits the Governor's signature and includes Washington, D.C.

This paper provides insight into how many workers could potentially be affected by raising Ohio's minimum wage above the federal and indexing it. This study updates and expands upon the April 2005 study called *Out of the Basement: Who Would Benefit from a Minimum Wage Increase in Ohio*, which examined the legislative proposal to raise Ohio's minimum wage to $7.15.[3]

Raising the minimum wage from the federally-mandated $5.15 an hour that applies to most Ohio workers to an indexed $6.85 would benefit 719,000 workers, bring many workers to a level that actually could bring a small family out of poverty, have substantial benefits for workers already earning more than $5.15, and ensure that inflation does not quickly erode the value of low-wage workers' paychecks.

Restoring Ohio's minimum wage to a level comparable to what it was in the past would again send a message that Ohio values its working families, and would send our state back toward the economic high road.

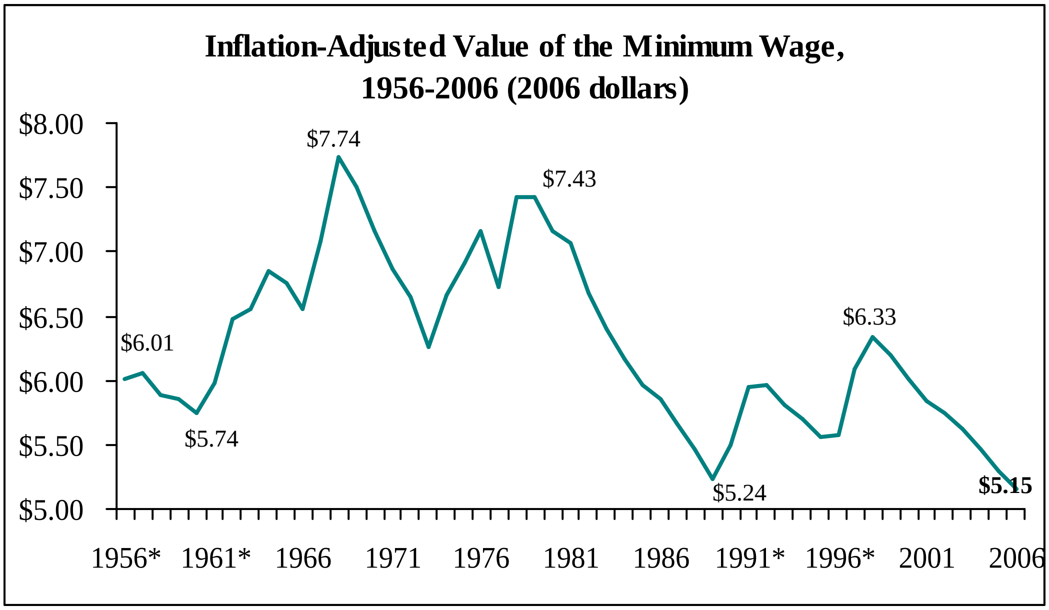
History

The 1938 Fair Labor Standards Act first established a wage floor or minimum wage for workers in the United States. Originally set at $0.25, equal to about $3.50 in 2006 dollars, Congress steadily increased the wage during the economic expansion of the 1950s and 1960s to a 1968 high of $7.74 in today's dollars. [4] Because the federal minimum wage is not indexed to inflation, it loses value over time, until Congress acts again to raise the level. Recent state initiatives, including the proposal being circulated for the Ohio ballot, address this issue by indexing their state minimums to inflation. Since the 1997 raise to $5.15, the rising cost of living has eroded the real value of the minimum wage to its lowest point in more than fifty years. Figure 1 tracks the value of the minimum over the past fifty years in 2006 dollars, showing that since 1955, the previous low points have been higher than the current value in inflation-adjusted terms ($5.74 in 1960 and $5.24 in 1989 after a decade of decline).

[3] That paper is available at http://www.policymattersohio.org/out_of_the_basement.htm. For more on the methodology for this paper and the differences between the two papers, see Appendix A.

[4] We adjust past prices to inflation using the Consumer Price Index urban research series (CPI-U-RS) index to inflate dollars. This is generally considered a more cautious and conservative deflator than the urban index (CPI-U) which was previously used (and is still used by the Bureau of Labor Statistics). Had we used the CPI-U, the 1968 value would have been $9.02 in 2006 dollars, not $7.74.

Figure 1



Source: Economic Policy Institute (EPI) analysis of U.S. Department of Labor data. Values deflated using CPI-U-RS and using the CBO's prediction of 2.8% inflation for 2006.
* indicates that wage was raised during that calendar year, value reflects weighted average for year.

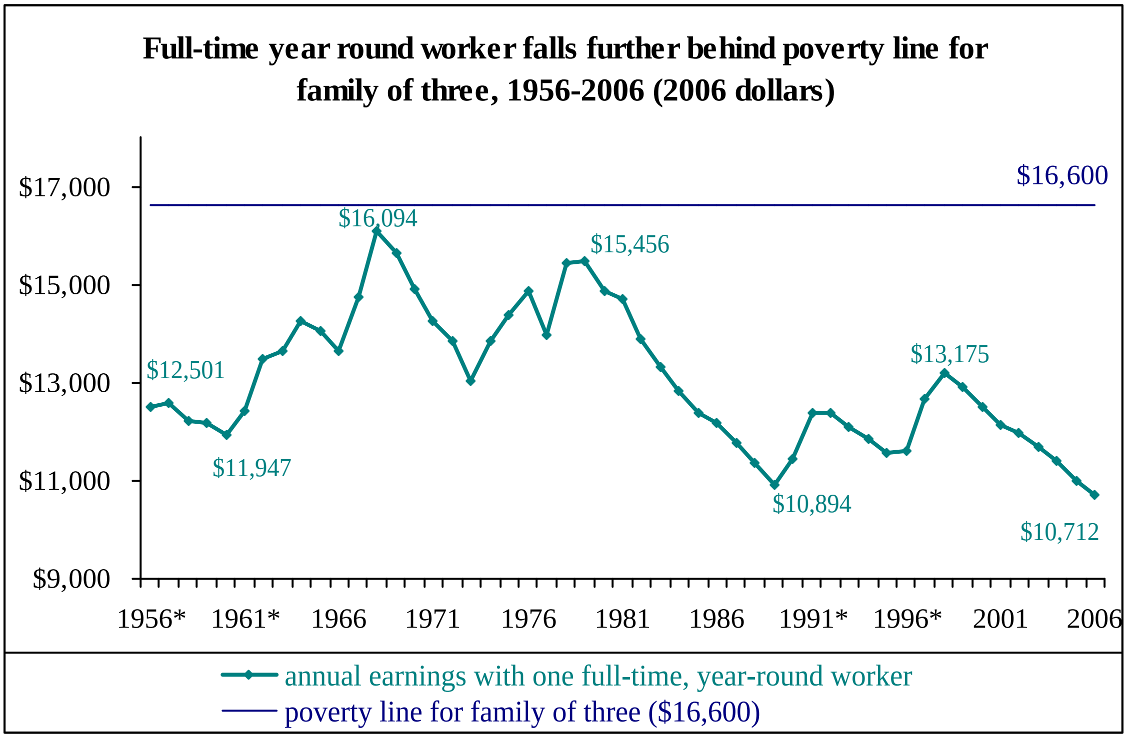
The federal minimum wage reached its highest point in 1968. Since then, wages of minimum wage workers have fallen by more than thirty percent in inflation-adjusted dollars. Today, one full-time earner with a family of three would fall 35.5 percent below the official 2006 federal poverty level ($16,600).[5] Figure 2, below, illustrates this growing gap between annual minimum wage earnings (the jagged green line) and the official poverty line for a family of three ($16,600 – the straight blue line).

Most analysts agree, however, that the official poverty line grossly understates actual costs of living. The Economic Policy Institute has estimated the cost of a "basic family budget" and the women's organization Wider Opportunities for Women has estimated "self-sufficiency standards," each of which are well above the official federal poverty line.[6] Thus, Figure 2 understates the gap between minimum wage work and even a very modest quality of life.

[5] Federal Register, Vol. 71, No. 15, January 24, 2006, pp. 3848-3849

[6] Depending on family size and community, these standards range from 1.5 to 3 times the federal poverty level. Somewhat dated basic family budget estimates for Ohio are available at: http://policymattersohio.org/pdf/ohiobudgets.pdf (accessed March 2006).

Figure 2



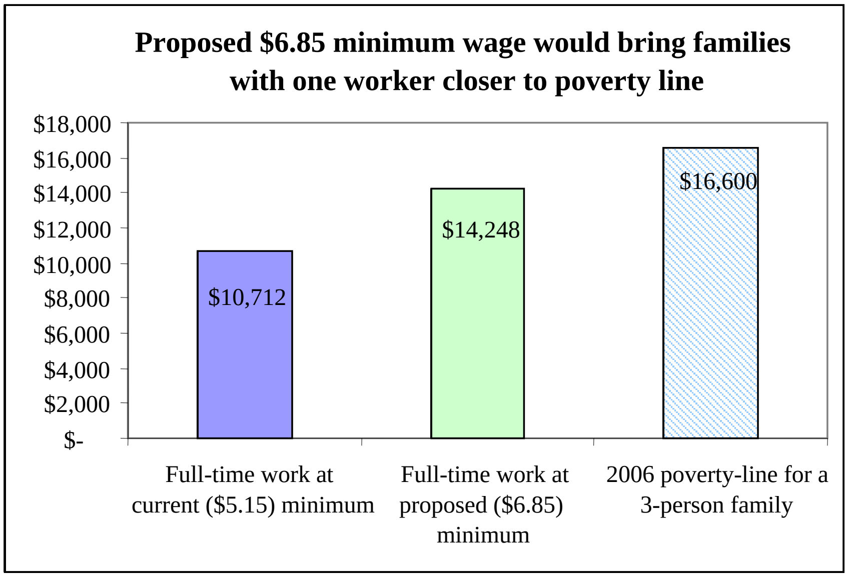
Source: EPI analysis of DOL data, deflated using CPI-U-RS and CBO 2.8 inflation prediction for 2006.
* indicates that wage was raised during that calendar year, value reflects weighted average for year

The current minimum wage isn't just insufficient to support a family of three—it falls short for single workers and smaller families. As mentioned, one full-time year-round worker earns $10,712 with a minimum wage pay rate of $5.15 an hour.[7] This is slightly above the 2006 official poverty line for a single individual ($9,800) but is significantly below the poverty line for even a two-person family ($13,200).

The Ohio proposal to increase the minimum wage would bring families who depend heavily on minimum wage earnings closer to or above the official poverty line, depending on family size and hours of work. At $6.85 an hour, family annual earnings would be $14,248, slightly more than the poverty line for a family of two, and 85.8 percent of the three-person poverty line. Individuals and two-person families working full time, or three-person families working more than 2423 hours a year would be able to escape the official poverty designation under the new wage. Figure 3 shows how the current minimum wage and the new minimum wage compare to the official poverty threshold.

[7] We define full-time, year-round work as 2080 hours a year – 40 hours a week for 52 weeks. This assumes that workers are either paid for or do not take any days off for sickness or vacation. Most minimum wage workers are not, in fact, provided paid leave for sickness or vacation.

Figure 3



Source: Author's calculations, Federal Register

Tipped employees

Under the federal and Ohio minimum wage laws, tipped employees can be paid a lower minimum wage than other workers. Seven states have set minimum wages for tipped employees that are either at or above the national minimum wage rate. All other states allow a "tip penalty," which enables employers to pay an hourly rate below the federal minimum under the assumption that wages will be supplemented by tips. The level of the tip penalty varies by state. Thirty-two states and the District of Columbia have wages somewhere between $2.13 and $5.15 for tipped employees. Ohio and ten other states have the lowest standards, allowing employees who garner at least $30 in tips each month to be paid as little as $2.13 an hour, the minimum required by federal law for tipped workers.

State of change

Legislation to raise the minimum wage is repeatedly proposed at the federal level, but none of these proposals have gained traction since the 1997 increase. Senator Ted Kennedy recently proposed increasing the minimum wage within two years to $7.25 an hour.[8] Like previous attempts, however, this seems unlikely to become law in the current U.S. Congress. However, state-level attempts to raise the minimum wage are being taken very seriously, by voters and legislators of both major political parties.

Twenty states, including Washington, DC as a state and including Michigan where the bill has not yet been signed into law, have set wage floors above the federal level of

[8] http://ga3.org/campaign/minwagecosponsor, accessed March 12, 2006.

$5.15. This compares to just five states that had a minimum above the federal as of 1997. Table 1 shows the current law in states that have established minimum wages above $5.15, including Michigan where the bill still must be signed.

Table 1

States with Minimum Wages Above Federal Level		
State	**2006 Wage**	**Scheduled increase or other interesting feature**
Washington	$7.63	Indexed to inflation
Oregon	$7.50	Indexed to inflation
Connecticut	$7.40	Will increase to $7.65 on 1/1/07
Vermont	$7.25	Indexed to inflation
Alaska	$7.15	
New Jersey	$6.15	$7.15 by October 2006, reviewed annually by committee
District of Columbia	$7.00	Automatically remains $1.00 above federal level
Michigan*	$6.95	Bill calls for increase to $7.15 in July 2007 and $7.40 in July 2008; must still be signed into law; governor expected to do so
California	$6.75	Governor and legislature have both announced intent to raise
Hawaii	$6.75	Will increase to $7.25 on 1/1/07
New York	$6.75	Will increase to $7.15 on 1/1/07
Massachusetts	$6.75	Remains at least ten cents above federal
Rhode Island	$6.75	
Illinois	$6.50	
Maine	$6.50	Governor expected to sign legislatively approved increase to $7
Florida	$6.40	Annual increase according to inflation
Delaware	$6.15	
Maryland	$6.15	Legislature overrode governor’s veto in January 2006
Minnesota	$6.15	
Wisconsin	$5.70	Will rise to $6.50 in 2006
* Not yet signed into law		

Source: Economic Policy Institute

Ballot Box

Raising the minimum wage has proven popular when taken directly to the voters. Minimum wage increases got 68 percent of the Nevada vote and more than 70 percent of the Florida vote in November 2004.

As of the beginning of March 2006, coalitions in seven states were working to increase the minimum wage through ballot initiatives. In one week in March, however, the Republican legislatures in both Michigan and Ohio sought to increase the minimum wage legislatively, despite having previously opposed such efforts. The Michigan legislature increased the wage by 44 percent, to $6.95 by October 2006 and to $7.40 by July 2008. The Ohio proposal merely brought the wage up to the federal level that applies to most workers already.

Assuming that the Michigan effort is taken off the ballot,[9] coalitions continue to gather signatures to place minimum wage increases on the ballot in Arizona, Arkansas, Colorado, Missouri, Montana, and Ohio. In Nevada, ballot initiatives must be passed twice, and a minimum wage increase will be voted on for a second time in 2006, after the previous 68.3 percent victory.

Legislative action – from both parties

In addition to ballot measures, several increases have passed legislatively with more than ten state legislatures taking action to create or further raise an existing state minimum wage in just the past year and a half. In New York and Maryland, legislators raised the wage by overriding governors' vetoes. The California governor, after repeatedly vetoing legislatively-passed increases with indexing, recently announced a plan to raise the minimum wage in two steps to $7.75 by July 2007. Four states saw their minimum wage rise in January 2005 because of past legislative action. In several states, bills are expected to pass or have passed at least one house of the legislature (these include Pennsylvania, North Carolina and New Mexico). In many other states, legislation has been introduced but was derailed in some other way before passage.

Inflation-indexing

Florida, Oregon, Vermont and Washington have all indexed their minimum wage to inflation, and the Nevada increase will also be indexed if re-approved. Nine other states (including DC) do not index their wage, but have put in place other mechanisms for a one-time or more frequent scheduled increase. New York, Maine, and Washington, D.C. passed additional increases after the first boost. The lack of indexing is the main difference between what legislators in Michigan just passed and what had been sought at the ballot box, and all current coalition efforts except Montana's include an indexing component. In some places where the higher minimum wage is not indexed, legislators are pushing for levels above the current floors (these include Massachusetts, Rhode Island and the previously mentioned California.)

In all, then, twenty states have passed higher minimum wages (including D.C. and Michigan) and many more have grassroots or legislative campaigns to set higher wages. About half (49.7 percent) of the U.S. population will be covered by a higher minimum wage when the Michigan increase is signed and implemented.

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[9] The status is currently unclear.

Ohio Efforts

Until the move in early March to adjust the Ohio rate to the federal, the state was one of only two in the country with a state minimum wage ($4.25) lower than the federal ($5.15), although the federal wage has always applied to almost all workers. [10] The federal law covers all firms that engage in interstate commerce or gross more than $500,000 a year. [11] About 1.9 percent of the state's employees, nearly 92,000 people, currently earn less than the federal minimum wage, according to the U.S. Department of Labor's Bureau of Labor Statistics. Of those workers, 61 percent work in food service. Others are laborers, farm workers, salespeople and administrative support employees.[12]

When the Ohio minimum wage was put in place in January 1974, the rate was equal to the federal rate. Four months later, Ohio fell behind the federal wage and has remained at or below the federal rate ever since. Both the federal and state minimum wage have declined dramatically in real value over the past thirty years and the federal minimum was last this low in value in 1955.

The proposal circulating for the Ohio ballot, which raises the wage to $6.85 in January 2007 and indexes the wage to inflation thereafter, would place Ohio roughly in the middle among states with higher minimum wages – eleven states will have wages higher than that level by then, two states currently scheduled to have a $6.75 wage are pushing for a higher rate, and seven states have minimum wages between $5.70 and $6.75.

Who Gains?

We find that 719,000 Ohio workers are likely to receive a raise if the minimum wage is increased to $6.85.[13] Of these, 297,000 currently earn less than $6.85 and will be directly affected with an increase to at least the new required level. An additional 423,000 are indirectly affected – already earning $6.85 or more but likely to nonetheless get a wage increase due to increased options for low-wage workers. Table 2 provides the number of Ohio workers who are likely to see a wage increase, by demographic and other characteristics.

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[10] The Kansas minimum wage is $2.65. Note that six states have no minimum wage law in place – employees in these states actually have fewer protections than Ohio workers have.
[11] The actual Ohio minimum wage depends on the employer's gross sales and can range from $2.80 - $4.25 for the 92,000 Ohio workers not covered by the federal minimum.
[12] Sheban, Jeffrey, and Catherine Candisky. "Minimum Wage in Ohio May Get Boost: Bill Eventually Would Bump Rate Above Federal Level." *Columbus Dispatch.* 10 Jan. 2004.
[13] The methodology for this paper is slightly different than the methodology of the previous paper on the topic by Policy Matters. The new methodology better accounts for the spillover effects on workers earning a low salary, but more than the new minimum. See Appendix A for more information about methodology.

Table 2

Number of workers in Ohio who would be likely to get a raise, by demographic and other characteristics	
	Affected workers
Total workers affected	719,000
Directly affected	297,000
Indirectly affected	423,000
Male	301,000
Female	418,000
White	594,000
Black	78,000
16 to 19 years	191,000
20 years and older	529,000
1-19 hours	159,000
20-34 hours	261,000
Full-time (35+ hrs.)	299,000
Retail trade sector	185,000
Leisure & hospitality sector	192,000
Sales occupation	166,000
Service occupation	273,000
Married	196,000
Parent	135,000

Source: EPI analysis of Current Population Survey (CPS) data.

Research has shown that some employers adjust the wages of employees earning just above the new minimum wage, in order to maintain pay scales that were in place prior to a minimum wage increase. Forthcoming research from the Economic Policy Institute shows that this “spillover effect” in the case of the Ohio proposal would be greatest for workers earning very close to $6.85 and would decline, phasing out completely around $9.00.

All in all, about 14 percent of Ohio workers can expect to see a raise if the minimum wage is increased. Those who will be directly affected – that is those earning under $6.85 prior to the increase – will see larger raises, about 80 cents an hour on average. Those already earning over the new minimum when it is imposed will, on average, get an estimated raise of about 26 cents an hour. Considering all affected workers together, the average affected worker was earning $6.82 an hour last year, would have been earning $7.08 by 2007 due to nominal wage growth, but can expect to instead earn $7.56, a 48 cent raise on average. For a full-time, year-round worker, this would raise annual earnings by about $1,000. Table 3 shows the percent of workers affected directly and indirectly, their average wage as of last year and at the time of the increase, and the average raise we predict.

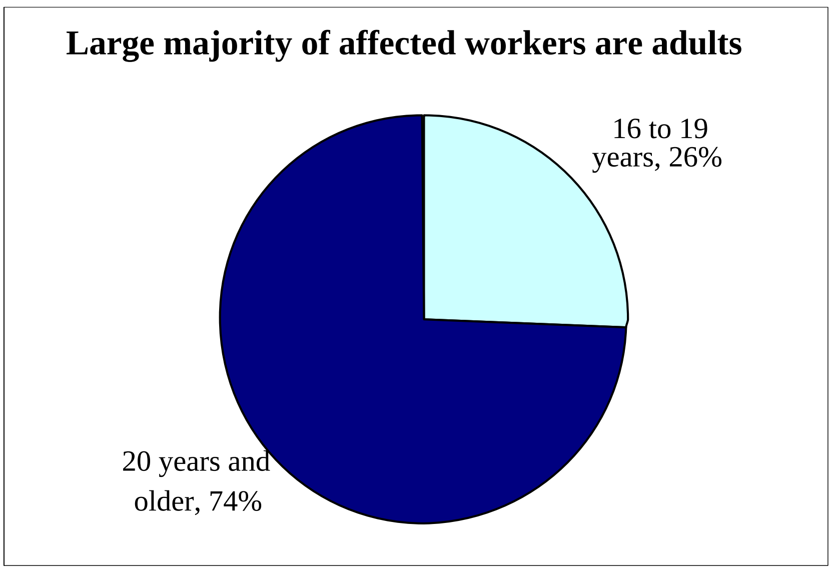
Table 3

Average affected workers – who are they and what raise will they get?				
Workers	Percent of all workers	Average wage		Average raise
		2005	Estimated 2007	
Directly affected	6%	$5.92	$6.09	$0.80
Indirectly affected	8%	$7.45	$7.78	$0.26
All affected	14%	$6.82	$7.08	$0.48

Source: EPI analysis of CPS data

About three quarters of these workers (74 percent) are age 20 or older, as Figure 4 shows. Although minimum wage jobs are often depicted as a brief character-building rung at the bottom of the career ladder, the Boston Federal Reserve Bank and the University of Michigan found that 40 percent of American families remained in the same income quintile throughout the 1990s and that 53 percent of those who started the decade in poverty remained in poverty.[14]

Figure 4

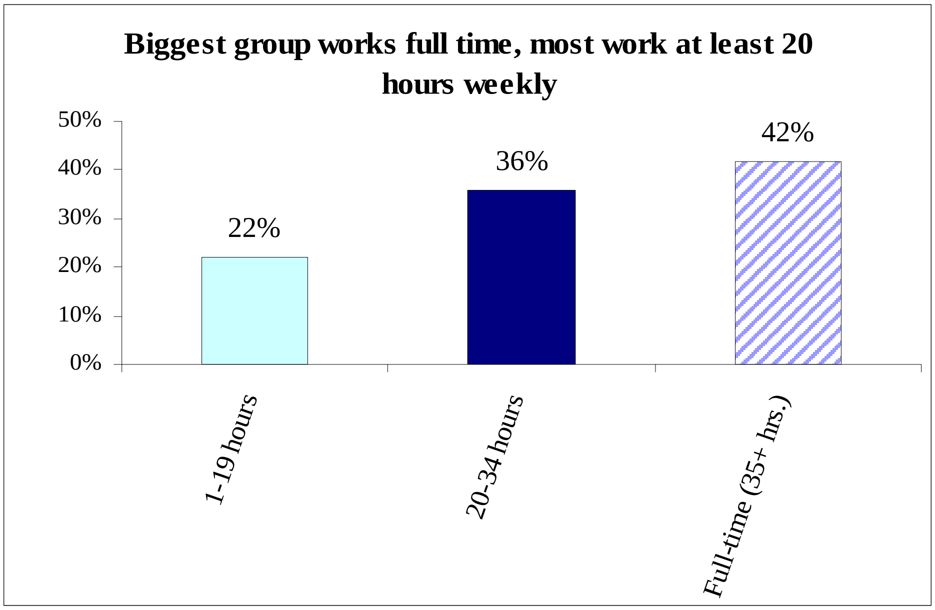


Source: EPI analysis of CPS data

The vast majority (78%) of workers who will get a raise work at least 20 hours a week. Forty-two percent work full time, as Figure 5 shows.

[14] Bernstein, Aaron. "Waking up from the American Dream." *BusinessWeek*. 1 Dec. 2003.

Figure 5



Source: EPI analysis of CPS data

More than one in four of these workers (28 percent) is married, and about one in five is a parent. Approximately 253,000 Ohio children have parents who would see a raise under this proposal. Not all affected employees are poor or support a family on their earnings alone. However, it is striking to note how much these workers contribute to family earnings. On average, families with workers who would see a raise rely on those workers for more than half of the family's weekly earnings.

An astounding percentage (38 percent) of families with low-wage earners rely entirely on those workers' earnings for weekly wage and salary income. In short, many of those affected by a hike play a significant role in their family's weekly income. Table 4 provides some detail.

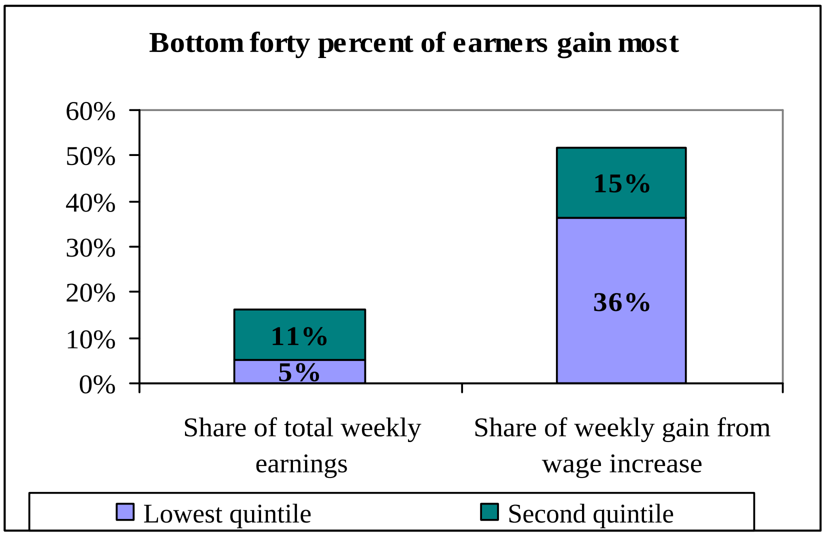
Table 4

How important are low-wage workers' earnings to their families?		
	Average share of earnings from affected workers	Share of families with 100% of earnings from affected workers
All families	52%	38%
Families with children	51%	39%
Number of children with parents affected by minimum wage increase		253,000

Source: EPI analysis of CPS data

More than half of affected workers (51 percent) come from the bottom forty percent of the household earnings spectrum, meaning that their households earn less than $737 a week on average, most of them significantly less. To learn more about which segments of the Ohio earnings distribution would benefit most from a minimum wage hike, we divided all Ohio families into five equal parts (referred to as fifths, quintiles, or groups of twenty percent). The largest share (36 percent) of the workers is in the poorest twenty percent of households (earning $285 a week on average). This lowest quintile of workers takes in only five percent of all weekly earnings, on average. Yet, this group would garner 36 percent of the wage increase associated with a minimum wage increase. The bottom forty percent of workers currently takes in less than sixteen percent of total wage and salary earnings, but would get more than half of the wage increases resulting from the $6.85 wage level, as Figure 6 shows.

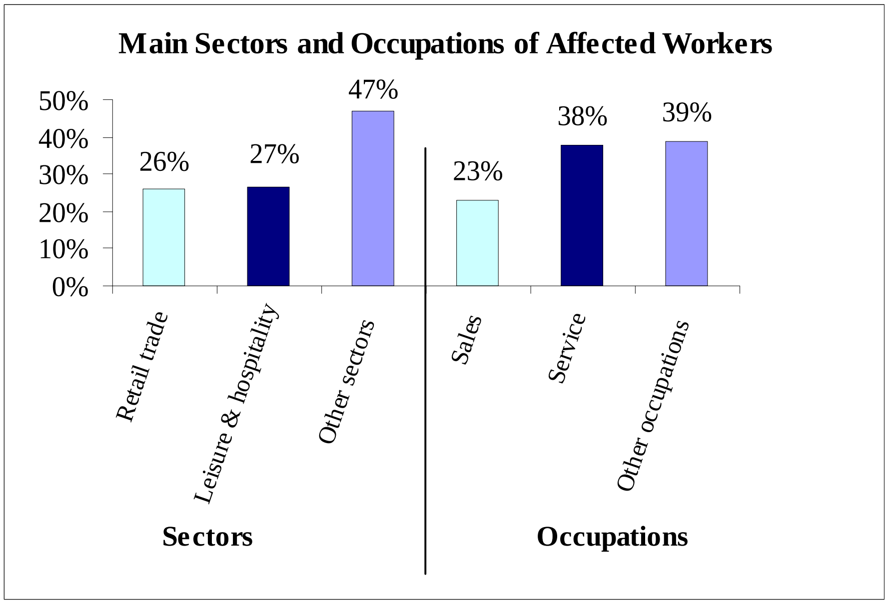
Figure 6



Source: EPI analysis of CPS data

Workers potentially affected by the minimum wage are concentrated in the Retail Trade and Leisure & Hospitality sectors, with about half of affected workers coming from one of those two sectors. Affected workers are also concentrated by occupation – more than half work in either sales or service occupations. Figure 7 shows the main sectors and occupations of affected workers.

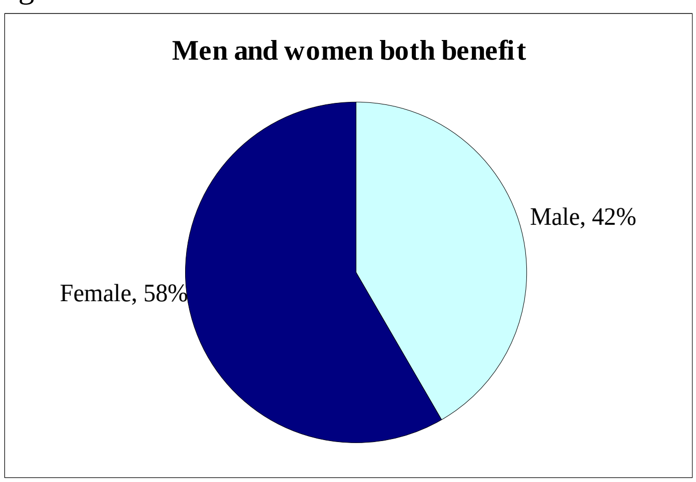
Figure 7



Source: EPI analysis of CPS data

A substantial majority (58 percent) of affected workers are women, but men and women both benefit, as Figure 8 shows.

Figure 8



Source: EPI analysis of CPS data

The share of black and white workers who would see gains from the increase is similar to the overall share of the workforce from each of these major racial groups. Fourteen percent of all white workers and 15 percent of all black workers could expect to see a raise under the proposal. Stated differently, whites make up 85 percent of Ohio's workforce and would comprise 83% of the beneficiaries from this proposal. Blacks are about ten percent of Ohio's workforce and would make up about 11 percent of those benefiting. Sample sizes did not permit us to make observations about the effect the proposal would have on Hispanic, Asian or other ethnic groups.

Conclusion

Since 1938, America has supported its workers by having minimum pay standards for jobs. As our nation's prosperity grew in the 1950s and 1960s, the quality of these standards increased. By the late 1960s, minimum wage jobs constituted a reasonable bottom rung in the labor market. Since 1968, the federal government has allowed the real value of a minimum wage job to deteriorate by more than thirty percent. Today's federal minimum wage of $5.15 an hour is lower in value than at any time in more than fifty years. If the minimum wage is supposed to provide a floor, then the current rate has descended to the basement.

Today's full-time minimum-wage earner brings in $10,712 annually, 35.5 percent below the official 2006 federal poverty level for a family of three ($16,600). Yet, these workers' earnings are crucial to many families' well-being. More than 250,000 children live in families with a worker at or near the minimum wage.

The current proposal to raise the Ohio minimum wage to $6.85 by January 2007 is comparable to proposals that have passed recently, either legislatively or at the ballot box, in states across the country. Twenty states, including neighboring Michigan where the governor is expected to sign a just-passed increase, have minimum wages above the federal level. In Florida and Nevada, voters overwhelmingly authorized minimum wage hikes, by 71.3 percent and 68.3 percent, respectively.

By raising and indexing our state minimum wage, Ohio would help more than 700,000 workers, reduce poverty, ensure that inflation does not quickly erode the value of worker paychecks, strengthen communities, and improve family well-being. At the same time, Ohio could again send a message that we value work, we support those who play by the rules, and we want to move toward an economy that works for all.

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Appendix A: Estimating wage effects of proposed minimum wage increases

The model

The first step is to calculate the effect of a minimum wage increase on average wages at different points in the wage distribution. To do this, we compiled a dataset using data from the Current Population Survey that contains average wage growth at various points in the wage distribution for each state in each year from 1984-85 to 2004-05. The dataset also contains data on state unemployment rates as well as identifiers for the year and state, which allow us to control for factors that are unique either to a single state (such as industrial make-up) or to a particular year (such as inflation).[15]

The key variable of interest is the change in the minimum wage. Past research has shown that the size of the "bite" of a minimum wage increase is strongly related to its economic impact. Therefore, the measure of a minimum wage increase that we use is the percentage of the workforce earning between that year's minimum wage and the following year's minimum wage during the year prior to the increase. This allows for the effect of a $1 increase in the minimum wage of a low-wage state to have a different effect than a similar increase in a high-wage state.

We then estimate an equation that uses the minimum wage increase, the unemployment rate, and state and year effects to estimate wage growth. The model finds that the effect of the minimum wage declines as you move up the wage distribution, but proves to be significant up to about the 20th percentile. These wage effects cannot be accounted for by the directly mandated raises required by the law, showing that the so-called "spillover effect" exists and is significant. It also shows, however, that it is rather modest and does not extend throughout the wage distribution. The theory behind this finding is that employers feel pressure to raise the wages of workers already earning above the new minimum wage in order to keep existing wage differentials.

Projecting forward

To model the effects of a minimum wage proposal, the first step is to estimate what each worker's wages would be in the absence of a minimum wage increase. The model described above lends itself well to this. We use Economy.com unemployment rate projections and assume that the state effects remain roughly similar and that year effects are roughly similar to the past few years. We are able to do this for various points in each state's wage distribution. We also use Economy.com employment growth projections to grow the workforce.

Estimating direct effects

For all workers whose predicted wage in 2007 is between the current and proposed minimum wages, we assume they will receive a raise directly due to the minimum wage. The direct effect for these workers is therefore the difference between their predicted 2007 wage and the proposed 2007 minimum wage.

Estimating average spillover effects

The next step is to estimate the average spillover effect for workers above the proposed minimum wage. This is estimated using the model described above and depends on the size of the direct effect. This is estimated separately for each point in the wage distribution.

Workers who were earning just below the proposed minimum wage are also given a spillover effect in accordance with their place in the wage distribution.

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[15] The model does not control directly for worker demographic characteristics. We found that while variables such as age, gender, and education are strong determinates of where one is in the wage distribution, they do not play a significant role in the wage growth at a narrow range of a state's wage distribution once state effects are controlled for.

Distributing the spillover effects
We make the assumption that within a given point in the wage distribution the spillover boost received by workers takes on a normal distribution ("bell curve") around the mean estimated above. This assumption, commonly made in statistics, means that, for example, if the mean boost for workers earning $7.00 is $0.50, then roughly 95% of workers will receive boosts between $0.25 and $0.75.[16]

Defining a meaningful spillover boost
It is likely that the wage boost received by many workers within the affected range will be very small and not particularly meaningful even if statistically significant. We have chosen to count only workers we expect to receive at least a 20 cent wage boost as a meaningful benefit. This would mean about $400 per year for a fulltime worker.

Given the mean boost estimated in the model and the assumption that the wage boosts are distributed normally at any given point in the wage distribution, we are able to estimate the number of workers that will receive meaningful boosts.

[16] This also requires us to estimate a standard deviation. We found that setting the standard deviation to be ¼ of the mean provides what we believe to be the best fit.

Policy Matters Ohio is a non-profit, non-partisan policy research institute dedicated to researching issues that matter to Ohio's working families. We seek to broaden the debate about economic policy in Ohio by providing Ohio's citizens, reporters and policy makers with essential tools to participate in public discussion. Ultimately, we believe that a broader debate will lead to a stronger and more just society. Other areas of inquiry for Policy Matters have included economic development, education, taxes, job growth, and unemployment.

3631 Perkins Avenue, Suite 4C - East • Cleveland, Ohio, 44114 • 216/361-9801
Columbus: 1372 Grandview Ave, Suite 242 • Columbus, Ohio 43212 • 614/486-4601

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