February 25, 2002

Hon. Bill Lockyer
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Tricia Knight
Initiative Coordinator

Dear Attorney General Lockyer:

Pursuant to Elections Code Section 9005, we have reviewed the proposed initiative measure known as the "California Workers' Livable Wage Initiative" (File No. SA2002RF0001, Amdt. #1-NS).

MAJOR PROVISIONS

The measure increases the state minimum wage from the current $6.75 per hour to $10.29 per hour, effective January 1, 2003. In addition, the measure requires the Industrial Welfare Commission to adjust annually the minimum wage rate based on a consumer price index. The first adjustment would be effective January 1, 2005.

The measure also exempts from the state minimum wage requirement family-owned businesses that have fewer than five employees and students under age 18 who work fewer than 20 hours per week.

Currently, most categories of employees are subject to the state minimum wage provisions. However, self-employed workers and professional and managerial workers are generally exempt from state and federal minimum wage laws.

FISCAL IMPACT

Impact on the Economy

This initiative would raise California's minimum wage by slightly over 50 percent. An increase of this magnitude would have significant effects on California's economy. Some of these effects are discussed below.

Direct Effects on Businesses. The minimum wage increase of the magnitude proposed by this measure would result in significantly higher wage costs for many businesses. Businesses would attempt to compensate for these higher costs by such means as raising prices, reducing other costs (including nonwage benefits to their employees), and/or scaling back their use of labor through automation. Businesses not able to compensate for the higher costs would face a reduction in profits and some would curtail operations in California. Overall, the measure would likely result in a reduction in employment and business activity in the state from what it otherwise would be.

Direct Effects on Low-Wage Employees. This measure would have varying effects on low-wage workers. Specifically:

- Those workers that were able to obtain and retain minimum wage jobs would experience substantial pay increases and thus would have more disposable income.
- Given the likely adverse impacts on businesses discussed above, however, many low-wage workers would probably find significantly fewer job opportunities available. These workers would experience a reduction in income and thus would have less disposable income.

Other Effects. In some cases where businesses were able to "pass along" part or all of the wage increase, the resulting increases in product prices would leave consumers and other businesses with less disposable income and less profits than otherwise. This would further reduce sales, employment, and income in California.

Impact on State and Local Revenues

The increased minimum wage would have offsetting impacts on state and local revenues. For example:

- ***Revenue Reductions.*** The higher wage costs resulting from the initiative would reduce revenues in several ways. First, the reduction in business profits reported on personal and corporate income tax returns by employers of minimum wage employees would reduce revenues from these two sources. This would occur even though minimum wage employees would have more taxable income to report, since their income tax rate would tend to be lower than for the employers. Second, the increased product prices for goods produced by minimum wage workers could leave consumers with less income available to spend on other goods, thereby reducing sales taxes from them. Third, the probable reduction in overall economic activity discussed above would lower collections from a variety of tax sources.

- ***Revenue Increases.*** The above losses would be partly offset to the extent that low-income employees allocated a large share of their increased wage earnings toward spending on goods subject to the sales tax. Similarly, to the extent that businesses were able to pass along their higher wage costs to consumers in the form of higher product prices on taxable purchases, this could also boost sales tax revenues.

On balance, we believe the initiative's revenue-reducing effects would outweigh its revenue-increasing effects, and thus that it would result in a net reduction in state and local revenues. While there are certain circumstances under which this initiative could result in revenue gains, we believe the most probable outcome is a net reduction in state and local revenues, most likely in the low hundreds of millions of dollars annually.

Impact on Public Sector Expenditures

Program-Specific Costs. State and local governments provide various services—primarily in the health and social services areas—that use low-wage, private sector employees:

- ***In-Home Supportive Services.*** The state would experience added costs of about $150 million in 2002-03, rising to about $350 million in 2003-04, for wage increases for approximately 275,000 service providers. Counties would face additional costs of about $90 million in 2002-03 and $225 million in 2003-04.
- ***Medi-Cal Nursing Facility Rates.*** The state would incur added annual costs in the low tens of millions of dollars to reimburse nursing facilities under the Medi-Cal program.
- ***Child Care Programs.*** Increased state costs for child care programs administered by the Departments of Education and Social Services could potentially be in the low hundreds of millions of dollars annually, due to increased wages of care providers.

Costs and Savings to Health and Social Services. To the extent the number of lower-wage job opportunities and therefore employment decline as a result of the measure, state and local governments could incur additional costs to provide various health and social services to the unemployed. These services include the Medi-Cal program, the California Work Opportunity and Responsibility to Kids (CalWORKs) program, and indigent health care services. The additional costs of these services are unknown.

These additional costs would be offset, to an unknown extent, by savings that result from reduced benefit levels provided to those who receive public assistance. This is because the increase in minimum wage would cause work earnings of program beneficiaries (or potential beneficiaries) to rise, thus lowering the benefit levels for which they are eligible. For example, higher incomes for working CalWORKs recipients would result in grant savings of roughly $40 million in 2002-03 and about $130 million in 2003-04.

Public Employee Costs. The increases in the minimum wage would directly increase costs to state and local governments for those employees making less than $10.29 per hour. There are relatively few public sector employees who make less than this amount. We estimate that added costs for these employees would be in the low tens of millions of dollars annually.

Other Cost Impacts. The higher minimum wage would increase state and local government costs in a number of other ways. For instance, to the extent that the measure results in a slight increase in inflation—as many studies suggest happens—the public sector could incur added costs for expenses indexed for inflation, such as certain welfare payments and building leases.

Summary of Fiscal Effects

This measure's increase in the minimum wage would result in the following major fiscal effects on state and local governments.

- Most probably a net reduction in state and local revenues potentially in the low hundreds of millions of dollars annually.
- Annual governmental costs—primarily in in-home supportive services—of about $800 million due to higher costs for goods and services.
- Unknown net costs or savings to provide health and social services to unemployed and low-wage workers, depending on the extent of job loss resulting from the measure.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

B. Timothy Gage
Director of Finance