

March 21, 2006

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

Attention: Ms. Patricia Galvan
Initiative Coordinator

Dear Attorney General Lockyer:

Pursuant to Elections Code Section 9005, we have reviewed the proposed statutory initiative regarding the minimum wage and labor laws (File No. SA2006RF0022).

BACKGROUND

Minimum Wage

Pursuant to state law, the current minimum wage in California is \$6.75 per hour. 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.

Work Schedules and Overtime Pay

Under state law, when an employee works more than eight hours in a day or more than 40 hours in a week, an employer typically must pay overtime wages of no less than 150 or 200 percent of the employee's regular rate of pay (depending on the number of hours worked). The law establishes several exemptions from these overtime pay requirements. Certain executive, administrative, and professional employees with a full-time monthly salary of at least two times the state minimum wage are exempt. Employees covered by certain collective bargaining agreements are exempt if the agreements provide for higher wage rates for overtime hours and a regularly hourly rate of pay of no less than 130 percent of the state minimum wage. In addition, upon the proposal of an employer, employees in a work unit may agree (with a two-thirds vote) to work for no more than ten hours per day within a 40-hour work week without overtime compensation.

PROPOSAL

Minimum Wage

The measure increases the state minimum wage from the current \$6.75 per hour to \$7.25 per hour effective July 1, 2007 and \$7.75 per hour effective July 1, 2008.

Work Schedules and Overtime Pay

Work Schedules. Under this measure, after submitting a written request and receiving approval from an employer, an individual employee could work under a schedule that includes up to ten hours per day with no overtime pay. Such an employee would receive overtime if he or she worked more than 40 hours per week or more than ten hours per day. The measure allows employers to inform employees of their willingness to consider requests for this type of work schedule. Employers would be prohibited from inducing such requests by promising employment benefits or threatening employees. Either the employee or employers could discontinue the alternative work schedule with at least a five day written notice. These provisions would not apply to employees already working under an alternative work schedule authorized in current state law, employees covered by a valid collective bargaining agreement, or public employees.

Overtime Pay. This measure expands the categories of employees that are exempt from the overtime pay requirements of the state's labor laws. Under this measure, managerial employees not required to receive overtime pay would be those who: (1) are compensated on a salary basis at a rate of not less than \$540 per week (\$13.50 per hour for a 40-hour work week); (2) have a primary job duty of managing an enterprise or a department or subdivision of an enterprise; (3) direct the work of two or more other employees on a regular basis; and (4) hire or fire other employees or whose recommendations are given particular weight in the hiring, firing, advancement, or promotion of other employees. In addition, certain workers with annual salaries of at least \$100,000 (including commissions and nondiscretionary bonuses) would be exempt from state overtime pay rules. This exemption covers workers performing executive, administrative, professional, managerial, and computer software responsibilities. (Based on the wording of the measure, it is unclear whether this exemption for workers paid at least \$100,000 per year also applies to other labor law requirements, such as workers' compensation.)

FISCAL IMPACT

Impact on Economy and Revenues

This initiative would raise California's minimum wage by 15 percent. An increase of this magnitude would have some effects on California's economy. The changes to overtime pay and work schedules could also have some effects.

Effects on Businesses. The minimum wage increase would result in somewhat higher wage costs for 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 reduce operations in California. Overall, the measure would likely result in some decline in employment and business activity in the state relative to what would otherwise have occurred.

Effects on Low-Wage Employees. The minimum wage provision would have varying effects on low-wage workers. Specifically:

- Those workers making less than the new minimum wage level would experience pay increases and thus would have more income.
- Given the potentially adverse impacts on businesses discussed above, however, some low-wage workers could find fewer job opportunities available. These individuals would experience a reduction in income.

Effects on Consumers. In some cases where businesses were able to "pass along" part or all of the costs of the wage increase, the resulting increases in product prices would leave consumers and other businesses with less income and less profits than otherwise.

Impacts on State and Local Revenues. The economic effects described above would have offsetting effects on state and local revenues. Increases in income for low-wage employees would increase personal income tax receipts. To the extent that this higher income was spent on taxable goods, sales tax receipts also could rise. In cases where the higher minimum wage is passed along by businesses to customers in the form of higher product prices, sales tax receipts on those products would also increase.

However, these gains would likely be more than offset by the negative impacts of the minimum wage increase on profits, employment, and spending in other areas of the economy. To the extent that higher wage costs reduce business profits, personal income and corporate tax receipts would decline. To the extent that the wage increases were passed along by businesses to their customers in the form of higher product prices,

consumers and businesses purchasing the higher-priced goods would have less discretionary income for other purchases, resulting in less sales taxes from them. Also, to the extent that the higher minimum wage resulted in less employment and economic activity in the state, taxes from a variety of sources would decline.

On balance, the economic and revenue factors related to the minimum wage described above would likely result in some net decline in state and local government revenues. In the context of overall state and local government revenues, any impact would probably not be significant.

Work Schedules and Overtime Pay. The measure's work schedule and overtime pay changes would decrease the number of private sector and public sector workers receiving overtime pay. In general, these changes could decrease wages received by certain categories of workers that would be exempted from overtime pay rules—resulting in an increase of business profitability. The magnitude of any such effects is unknown, but probably not significant. Any impact would partially offset some of the fiscal effects of the minimum wage increase described above.

Impacts on Public Sector Expenditures

State and local governments provide various services—primarily in the health and social services areas—using low-wage, private sector employees. The increase in the minimum wage could increase costs for these programs. The increase would be in the high tens of millions of dollars to over \$100 million per year. In addition, a small number of public sector employees make less than \$7.75 per hour. The added state and local government costs for these employees would be a few million dollars annually.

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 program, and indigent health 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.

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 would result in the following fiscal effects on state and local governments:

- Annual state and local government costs due to the minimum wage increase—primarily in health and child care programs—in the high tens of millions of dollars to over \$100 million.
- Potential net reduction, but probably not significant, in annual state and local government revenues.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

Michael C. Genest
Director of Finance