Department of Legislative Services

Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 543 (Senator Madaleno, *et al.*)
Finance

Labor and Employment - Payment of the Minimum Wage Required (Fight for Fifteen)

This bill phases in an increase in the State minimum wage to $15.00 per hour by fiscal 2024. Beginning on July 1, 2024, the minimum wage may increase further as it is indexed to inflation. The bill eliminates specified subminimum wages and phases out the tip credit by July 1, 2026, that employers can apply against the direct wages paid to employees classified as tipped employees. Additionally, the Governor's proposed budget for the Developmental Disabilities Administration (DDA) of the Maryland Department of Health must include specified rate increases for community services providers over the funding provided in the prior year's legislative appropriation beginning in fiscal 2020.

Fiscal Summary

State Effect: State expenditures (52% general funds, 48% federal funds) increase by $87.6 million in FY 2020, escalating to $341.9 million in FY 2023 due to the cumulative effect of rate increases for community services providers; federal fund revenues increase correspondingly. State expenditures (all funds) increase by *at least* $8.5 million in FY 2020 for additional payroll costs, rising to at least $65.4 million in FY 2023 (amounts not reflected below); federal fund revenues may cover a portion of these costs. General fund expenditures increase by $194,300 in FY 2019 for enforcement, with ongoing costs. General fund revenues increase minimally beginning in FY 2020. **This bill establishes a mandated appropriation beginning in FY 2020.**

($ in millions)	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
FF Revenue	$0	$42.1	$79.0	$119.6	$164.1
GF/FF Rev.	$0	-	-	-	-
GF Expenditure	$0.2	$45.7	$85.8	$129.8	$178.0
FF Expenditure	$0	$42.1	$79.0	$119.6	$164.1
GF/SF/FF/HE Exp.	$0	-	-	-	-
Net Effect	($0.2)	($45.7)	($85.8)	($129.8)	($178.0)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate increase; (-) = indeterminate decrease

Local Effect: Local government expenditures increase significantly beginning in FY 2020. Any change in local government tax revenues cannot be reliably projected but is expected to be minimal.

Small Business Effect: Meaningful.

Analysis

Bill Summary: For fiscal 2020, the Governor's proposed budget for DDA must include a 7.0% rate increase for community services providers over the funding provided in the prior year's legislative appropriation. For fiscal 2021 through 2024, the Governor's proposed budget for DDA must include an annual 5.5% rate increase for community services providers over the funding provided in the prior year's legislative appropriation. For fiscal 2025 and every year thereafter, the Governor's proposed budget for DDA must include an annual rate increase for community services providers at least equal to the indexed increase percentage of the State minimum wage.

The bill specifies that, unless the federal minimum wage is set at a higher rate, the State minimum wage is as follows:

- $11.00 per hour as of July 1, 2019;
- $12.00 per hour as of July 1, 2020;
- $13.00 per hour as of July 1, 2021;
- $14.00 per hour as of July 1, 2022; and
- $15.00 per hour as of July 1, 2023.

Beginning on July 1, 2024, and in subsequent fiscal years, the State minimum wage is the rate determined and announced by the Commissioner of Labor and Industry. Generally, the rate will be the prior-year rate plus the average percentage increase, based on the most recent 12-month period, in the Consumer Price Index (CPI) for the Washington-Baltimore metropolitan area (or a successor index that is published by the U.S. Bureau of Labor Statistics (BLS)). An increase in the State minimum wage must be rounded to the nearest multiple of five cents. However, if the CPI does not change during a given year, or decreases, the minimum wage remains at the same rate as that of the prior year. The commissioner must determine and announce the State minimum wage that will be in effect for the upcoming fiscal year by October 1 of each year.

The tip credit that employers can apply against the direct wages paid to employees classified as tipped employees may not exceed the minimum wage less:

- $3.63 per hour as of July 1, 2018;
- $5.25 per hour as of July 1, 2019;
- $7.50 per hour as of July 1, 2020;
- $9.00 per hour as of July 1, 2021;
- $10.50 per hour as of July 1, 2022;
- $12.00 per hour as of July 1, 2023;
- $13.50 per hour as of July 1, 2024; and
- $15.00 per hour as of July 1, 2025.

Beginning July 1, 2026, an employer may not include a tip credit amount as part of an employee's wage and must pay an employee a wage that is at least equal to the State minimum wage.

An employer may no longer pay 85% of the State minimum wage rate to employees younger than age 20 for the first six months of employment or to employees who work for specified amusement, recreational, or swimming pool establishments.

Current Law:

Maryland Wage and Hour Law

The Maryland Wage and Hour Law is the State complement to the federal Fair Labor Standards Act (FLSA). State law sets minimum wage standards to provide a maintenance level consistent with the needs of the population. State law specifies that an employee must be paid the greater of the federal minimum wage (which is currently $7.25 per hour) or $9.25 per hour. Under Chapter 262 of 2014, the State minimum wage is scheduled to increase to $10.10 per hour as of July 1, 2018.

However, an employer may pay an employee a wage that equals 85% of the State minimum wage for the first six months that the employee is employed if the employee is younger than age 20. Additionally, an employer of an amusement or a recreational establishment, including a swimming pool, that meets specified conditions may pay an employee a wage that equals the greater of $7.25 or 85% of the State minimum wage. Exceptions to the minimum wage requirement also exist for a training wage and a disabled employee of a sheltered workshop under specified conditions.

The Maryland Wage and Hour Law and minimum wage requirements do not apply to certain categories of employees, including those defined as administrative, executive, or professional; certain seasonal employees; part-time employees younger than age 16; salesmen and those who work on commission; an employer's immediate family; drive-in theater employees; employees training in a special education program in a public school;

employees of an establishment that sells food and drink for on-premises consumption and has an annual gross income of $400,000 or less; employees employed by an employer who is engaged in canning, freezing, packing, or first processing of perishable or seasonal fresh fruits, vegetables, poultry, or seafood; and certain farm workers.

The employer of a tipped employee is allowed a tip credit that can be applied against the direct wages paid by the employer. The employee can be paid tipping wages so long as the wages plus the tips received equal at least the minimum wage, the employee retains all tips, and the employee customarily receives more than $30.00 a month in tips. The tip credit is equal to the State minimum wage, less $3.63. Thus, the tip credit increases as the minimum wage increases, and the wage paid by employers to tipped employees remains $3.63, as long as their wages plus tips equal the minimum wage. The State and local governments are not considered employers under the tip credit provisions of the Maryland Wage and Hour Law.

If an employer pays less than the wages required, the employee may bring an action against the employer to recover (1) the difference between the wage paid to the employee and the wage required; (2) an additional amount equal to the difference as liquidated damages; and (3) legal fees. The court must award these differences in wages, damages, and counsel fees if the court determines that an employee is entitled to recovery. However, if an employer shows to the satisfaction of the court that the employer acted in good faith and reasonably believed that the wages paid to the employee were not less than the required wages, then the court must award liquidated damages of an amount less than the difference in wages or no liquidated damages.

A person who violates the Maryland Wage and Hour Law is guilty of a misdemeanor and on conviction is subject to a fine of up to $1,000.

Federal Fair Labor Standards Act

With some exceptions, similar to State law, FLSA requires that workers be paid a minimum hourly wage and that overtime compensation be paid to employees who work more than 40 hours in a week.

Mandated Rate Increases

In fiscal 2016 through 2019, the Governor’s proposed budget for DDA must include an annual 3.5% rate increase for community services providers over the funding provided in the prior year’s legislative appropriation. A portion of the funds may be allocated to address the impact of an increase in the State minimum wage on wages and benefits of direct support workers employed by community providers licensed by DDA. The

Governor's proposed budget for fiscal 2016 and thereafter for community services providers must be presented in the same manner as provided for in the fiscal 2015 budget.

Background: As of January 2018, as shown in **Exhibit 1**, 29 states, including Maryland, and the District of Columbia mandate a minimum wage higher than the federal minimum wage of $7.25 per hour, with rates ranging from $0.25 to $5.25 above the federal rate. Eight of these states (Alaska, Florida, Minnesota, Missouri, Montana, New Jersey, Ohio, and South Dakota) automatically increased their minimum wage rate based on the cost of living. Five states had no mandated minimum wage, another 2 had a minimum wage set lower than the federal minimum wage, and the remaining 14 states used the federal minimum wage. Unless a state has a higher minimum wage rate, the federal minimum wage rate applies.

Exhibit 1
States with Higher than Federal Minimum Wage, as of January 2018

State	Rate	State	Rate
District of Columbia	$12.50	**Maryland**	**$9.25**
Washington	11.50	Michigan	9.25
California	11.00	Nebraska	9.00
Massachusetts	11.00	South Dakota	8.85
Arizona	10.50	West Virginia	8.75
Vermont	10.50	New Jersey	8.60
New York	10.40	Arkansas	8.50
Oregon	10.25	Montana	8.30
Colorado	10.20	Ohio	8.30
Connecticut	10.10	Delaware	8.25
Hawaii	10.10	Florida	8.25
Rhode Island	10.10	Illinois	8.25
Maine	10.00	Nevada	8.25
Alaska	9.84	Missouri	7.85
Minnesota	9.65	New Mexico	7.50

Source: U.S. Department of Labor

Local Jurisdiction Labor Laws

Montgomery and Prince George's counties have local minimum wage laws of $11.50 per hour. The county minimum wages for Montgomery and Prince George's counties do not apply to an employee who is exempt from the minimum wage requirements of the

Maryland Wage and Hour Law or the federal FLSA or to an employee who is younger than age 19 and is employed no more than 20 hours in a week. Montgomery County passed legislation in 2017 to gradually increase its minimum wage so that employers with at least 51 employees are required to pay a minimum wage of $15.00 per hour effective July 1, 2021; mid-sized employers are required to pay a minimum wage rate of $15.00 per hour effective July 1, 2023; and employers with less than 11 employees are required to pay a minimum wage of $15.00 per hour effective July 1, 2024, and the county indexes the minimum wage rates to inflation. An employer may pay a wage equal to 85% of the county minimum wage to an employee younger than age 20 for the first six months that the employee is employed.

Baltimore City enacted a city minimum wage rate in 1964, which was challenged in the State Court of Appeals in *Mayor of Baltimore v. Sitnick*, 254 Md. 303, 255 A.2d 376 (1969). The court found that the State's minimum wage rate did not preempt Baltimore's minimum wage law since Baltimore's law supplemented the State law by setting a higher rate. Baltimore City still has its own minimum wage statute with an enforcement commission, which currently enforces the State minimum wage rate in the city.

Minimum Wage Effects on the Economy

There is much debate on how raising the minimum wage affects the economy. Positive impacts on the economy may include (1) increases in personal income; (2) decreases in employee turnover; (3) increases in local consumption; (4) higher labor force participation rates; (5) decreases in social welfare costs; and (6) higher levels of technological development, investment, and productivity.

However, on the downside, raising the minimum wage may (1) decrease demand for labor; (2) increase inflation from employers passing higher employee costs onto the consumer; (3) cause wage compression; (4) reduce local competitiveness; and (5) have disemployment effects. The disemployment effects happen when businesses hire fewer low-wage workers in response to an increase in the minimum wage; benefits to low-wage workers from increased wages may be offset by a reduction in hours worked or increased unemployment.

Tipped Employees

According to the U.S. Department of Labor, 7 states required employers to pay workers the full state minimum wage before tips in 2018 (Alaska, California, Minnesota, Montana, Nevada, Oregon, and Washington). Employers could pay workers the federal tipped minimum wage of $2.13 per hour in 17 states. The remaining states, including Maryland, allowed employers to pay tipped employees a minimum wage rate that is higher than the federal tipped minimum wage of $2.13 per hour but lower than the state's minimum wage.

State Revenues: General fund tax revenues may increase minimally from increasing the State's minimum wage beginning in fiscal 2020. Individuals earning minimum wage likely have low, if any, State income tax liability so raising the minimum wage only has a minimal effect on State income tax revenues. Any increase in personal income tax revenue is likely offset from diminished revenues from businesses with higher payroll expenses and from potentially a decrease in demand for labor. Given that raising the minimum wage boosts the purchasing power of minimum wage workers and generates new consumer spending, general fund sales tax revenues may increase minimally.

General fund revenues may increase minimally from a higher number of penalties paid by employers who are found by the Department of Labor, Licensing, and Regulation (DLLR) to be in violation of the Maryland Wage and Hour Law.

As noted below, federal fund revenues increase to cover the federal fund share of the rate increase for community services providers and *may* increase to cover a small portion of the additional payroll costs incurred by the State.

State Expenditures: The bill's expenditure effects for the minimum wage increase, administrative costs, and rate increases for DDA providers are addressed separately in this section.

Minimum Wage Increase

State expenditures (all funds) increase significantly as a result of incrementally raising the State minimum wage to $15.00 per hour by July 1, 2023; **Exhibit 2** displays some of the additional wages that must be paid to State employees in fiscal 2020 through 2023 under the bill.

Current law has the minimum wage rate set at $10.10 per hour beginning in fiscal 2019, so State expenditures increase by $8.5 million in fiscal 2020, which is the total wage effect of the difference between $10.10 and the $11.00 wage rate established under the bill. Expenditures in future years are calculated based on the difference between the $10.10 minimum wage rate that will be required under current law versus the rates under the bill so, by fiscal 2023, State expenditures increase by $65.4 million. These costs do not take into account any wage adjustments to internal salary ladders or increases in other compensation tied to wages. The State may increase wages for an employee who currently earns just above $11.00 per hour in fiscal 2020 or just above $14.00 per hour in fiscal 2023 and has more job responsibilities than a minimum wage employee. Any such wage adjustments further increase the State's expenditures, potentially significantly. To the extent that the State currently pays 85% of the State minimum wage to employees younger than age 20 for the first six months of employment, the State's expenditures may increase in fiscal 2019.

Exhibit 2
Effect of Phasing in a $15.00 Minimum Wage on State Employees
Fiscal 2020-2023

Additional Staffing Costs	**FY 2020**	**FY 2021**	**FY 2022**	**FY 2023**
Senior Citizen Aides	$174,057	$367,757	$566,917	$767,897
TSHRS Employees	0	0	191,138	723,341
MTA Union Employees	0	1,830	7,737	16,057
TSHRS Contractual/Temporary Employees	0	0	43,788	169,331
SPMS University Employees	1,893,837	4,384,858	7,112,450	9,996,364
Hourly/Contractual Employees within SPMS	130,229	457,783	1,123,623	2,219,006
Salaried Employees within SPMS	6,747	168,716	695,517	1,993,977
USM Employees	6,332,703	14,518,577	28,773,145	49,553,813
Increase in Expenditures	**$8,537,573**	**$19,899,521**	**$38,514,315**	**$65,439,786**
Federal Fund Revenues	174,057	367,757	566,917	767,897
Net Increase in Expenditures	**$8,363,516**	**$19,531,764**	**$37,947,398**	**$64,671,889**

MTA: Maryland Transit Administration
SPMS: State Personnel Management System
TSHRS: Transportation Service Human Resources System
USM: University System of Maryland

Source: Department of Legislative Services

Administrative Expenses

The bill creates additional responsibilities for DLLR's Division of Labor and Industry by gradually phasing out the tip credit and providing for subsequent increases in the minimum wage. These changes are expected to significantly increase the number of inquiries and complaints related to payment of the minimum wage. DLLR cannot fully absorb the additional workload within existing resources and requires additional staff to respond to the increase in inquiries and complaints prompted by the bill.

Thus, general fund expenditures increase for DLLR by $194,337 in fiscal 2019, which accounts for the bill's October 1, 2018 effective date. This estimate reflects the cost of hiring two DLLR wage and hour investigators to conduct outreach, respond to inquiries, investigate complaints, and enforce the new requirements. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Regular Positions	2
Regular Salaries and Fringe Benefits	$77,719
Operating Expenses	116,618
Total FY 2019 State Expenditures	**$194,337**

Future year expenditures reflect full salaries with annual increases and employee turnover and ongoing operating expenses.

Mandated Rate Increases for DDA Community Services Providers

The bill establishes a mandated appropriation beginning in fiscal 2020. Beginning in fiscal 2020, the Governor's proposed budget for DDA *must* include an annual specified rate increase for community services providers over the funding provided in the prior year's legislative appropriation. A portion of the funds *may* be allocated to address the impact of an increase in the State minimum wage on wages and benefits of direct support workers employed by community providers licensed by DDA.

Accordingly, DDA expenditures increase by an estimated $87.6 million (52% general funds, 48% federal funds) in fiscal 2020 and by an estimated $341.9 million (52% general funds, 48% federal funds) in fiscal 2023 to provide the *mandated* rate increases to community services providers. (Federal fund revenues increase correspondingly.) The compounding effect of the 7.0% and then 5.5% rate increases on expenditures for fiscal 2020 through 2023 is shown in **Exhibit 3**. The fiscal 2019 budget includes $1.2 billion (total funds) for contractual expenses for DDA community services providers.

Exhibit 3
Impact of Annual Rate Increase for Developmental Disabilities Providers
Fiscal 2020-2023
($ in Millions)

	FY 2020	FY 2021	FY 2022	FY 2023
General Fund Expenditures	$45.57	$85.62	$129.60	$177.78
Federal Fund Expenditures	42.07	79.03	119.63	164.11
Total Expenditures	**$87.64**	**$164.65**	**$249.23**	**$341.89**

Source: Department of Legislative Services

Local Fiscal Effect: Expenditures could increase significantly by fiscal 2023 for some local governments to pay employees (typically part-time or contractual employees) the minimum wage rates specified in the bill. For example, Calvert County estimates expenditures increasing by $1.75 million to pay 330 employees the State minimum wage rate in fiscal 2020.

Small Business Effect: Small businesses in the State that employ minimum wage or low-wage workers experience significant increases in their labor costs due to the bill. The impact is even greater for small businesses that employ tipped employees and for employers that currently pay 85% of the State minimum wage to employees younger than age 20 for the first six months of employment and to employees in specified amusement, recreational, and swimming pool establishments.

BLS reports there were 43,090 waiters and waitresses in the State in 2013, earning median hourly wages of $8.71. By phasing out the tip credit and raising the State minimum wage, an employer must pay a tipped employee an hourly wage rate of at least $15.00 (plus the indexed inflation if applicable) instead of $3.63 by July 1, 2026. Thus, the bill has a significant adverse impact on small businesses that pay tipped employees.

To the extent that higher wages increase worker productivity, businesses would be less affected by the provisions of the bill. Additionally, minimum wage workers tend to have a low saving rate, so increasing their wages could lead to additional consumer spending for small businesses.

Additional Comments: Beginning July 1, 2024, the State minimum wage rate is indexed to inflation based on the CPI for the Washington-Baltimore metropolitan area or a successor index published by BLS. However, BLS is revising the CPI geographic sample. The CPI for the Washington-Baltimore metropolitan area will no longer be available beginning in 2018 but, instead, is replaced with two new CPIs: a CPI for the Baltimore metropolitan area and a CPI for the Washington metropolitan area. Both indexes contain Maryland counties. The CPI for the Baltimore metropolitan area contains Baltimore City and Anne Arundel, Baltimore, Carroll, Harford, Howard, and Queen Anne's counties. The CPI for the Washington metropolitan area contains Calvert, Charles, Frederick, Montgomery, and Prince George's counties.

BLS notes that metropolitan area indexes have a relatively small sample size and, therefore, are subject to substantially larger sampling errors. Metropolitan area and other subcomponents of the national indexes (regions, size-classes) often exhibit greater volatility than the national index. BLS recommends that users adopt the U.S. city average CPI for use in escalator clauses.

Additional Information

Prior Introductions: None.

Cross File: HB 664 (Delegate Hettleman, *et al.*) - Economic Matters.

Information Source(s): Calvert and Montgomery counties; Maryland Association of Counties; City of Takoma Park; Maryland Municipal League; Comptroller's Office; Judiciary (Administrative Office of the Courts); University System of Maryland; Department of Budget and Management; Maryland Department of Health; Department of Labor, Licensing, and Regulation; Maryland Department of Transportation; U.S. Department of Labor; Department of Legislative Services

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Analysis by: Heather N. Ruby

Direct Inquiries to:
(410) 946-5510
(301) 970-5510