Insight

Case Study: Minimum Wage Meets the Military

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What happens when you increase the minimum wage on military bases? It turns out that jobs disappear and businesses shut down at an alarming rate. After implementing regulations that increased the minimum wage on military bases last year, the Department of Labor (DoL) decided in April to exempt fast-food workers from the new rules. This only came after concessionaries started rapidly shutting down, leaving many out of work. Unlike a private business, concessionaries on bases can't raise prices freely, making it impossible for them to bear the higher labor cost. While it is unclear what DoL plans to do next, the events that have transpired since last year provide a unique case study for the labor market effects of raising the minimum wage.

RULE CHANGES AND THE FALLOUT

In 2013, DoL enacted rules raising the minimum wage required for fast food workers on federal contracts. Under the Service Contract Act (SCA), any worker under a service federal contract over $2,500 must be paid at least a minimum wage and receive a minimum level of fringe benefits, both of which are determined by the Secretary of Labor. Prior to 2013, fast-food workers were exempt from such requirements. Moreover, in June of 2013, DoL increased the health and welfare fringe benefits for all service contract workers to $3.81 per hour from $3.71 per hour in 2012.

Between the minimum wage increases and the new required payment of fringe benefits, these rule changes effectively imposed a massive wage hike for fast-food restaurants under federal contracts. According to the Navy, fast-food restaurants in Florida, California, and Virginia faced minimum wage hikes ranging from 72 to 76 percent. In one area of California, for instance, the combination of the minimum wage increase and the new $3.81 per hour health and welfare payments resulted in fast-food restaurants increasing their effective minimum wage from $7.25 to $12.79 per hour.

These wage hikes became especially problematic for federally contracted fast-food restaurants located on military bases because under most contracts they are not permitted to increase prices beyond those at nearby, similar fast-food restaurants. As a result, when the minimum wage for their employees increased, the restaurants were not able to offset the higher cost with price increases.

The straw that broke the camel’s back was when President Obama signed an executive order in February of this year that raised the minimum wage to $10.10 per hour for all federal contract workers (effective 2015). With even more mandated labor costs set to come, several fast-food restaurants on military bases started shutting down at an alarming rate. In March alone, McDonald’s restaurants shut down on three Navy bases and another will close on a Marine base. The military estimates that the new rules could force 390 fast-food restaurants on military bases to close and 5,750 workers to lose their jobs. These rules have also forced the Navy and Marine Corps to suspend 74 contracts and they estimate the rules will cost $27 million per year in restaurant profits.

With so many restaurants closing or planning to close, last month DoL decided to once again exempt fast-food restaurants from SCA wage and benefits standards. However, DoL plans to review the rules and may reissue them in the future for fast-food restaurants, continuing to threaten employment on military bases.

IMPLICATIONS

It is still uncertain where DoL will go from here, but this string of events illustrates important consequences to increasing the minimum wage. It is clear that there are at least two primary costs to a higher minimum wage: fewer jobs, higher prices, or both. In the case of fast-food restaurants on military bases, job losses occurred in various forms. While some restaurants were likely forced to fire workers, others simply had no option but to close up shop. Meanwhile, the 74 suspended contracts also resulted in lower job creation, as job growth on military bases likely slowed dramatically.

The fact that rigid pricing rules on military bases made the job losses so much more intense only illustrates that the second main cost of minimum wage hike is indeed higher prices (at least in the fast-food industry). This hurts consumers who, years after the Great Recession ended still face flat income growth. In the fast-food industry these consumers are often low-income families trying to save money on low cost, high-calorie meals.

CONCLUSION

DoL’s new wage rules for federally contracted fast-food restaurants on military bases provide a perfect case study on the minimum wage’s labor market effects. Our armed forces should not be forced to lose fast-food restaurants, which mainly employ military spouses and veterans. Moreover, with real GDP only growing at an annual rate of 0.1 percent so far this year, the last thing our economy needs is another mandate with so many negative effects. It’s time to move on from minimum wage and focus on solutions that actually increase work and grow the economy.