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To: The Council

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Subject: **ANALYSIS OF THE IMPACT ON THE CITY OF LOS ANGELES OF THE PROPOSED MINIMUM WAGE FOR HOTEL WORKERS**

Attached for your consideration is a report prepared for the City by Blue Sky Consulting Group titled Hotel Minimum Wage: Analysis of the Impact on the City of Los Angeles of the proposed Minimum Wage for Hotel Workers. This report was prepared at the request of the Economic Development Committee in consideration of Council File 14-0223 concerning a living wage of \$15.37 per hour for hotel workers in hotels with 100 rooms or more. The Chief Legislative Analyst and the City Administrative Officer will release a report on this subject at a later date.

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Blue
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CONSULTING GROUP

Hotel Minimum Wage

Analysis of the Impact on the City of Los Angeles of the
Proposed Minimum Wage for Hotel Workers

June 3, 2014

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ACKNOWLEDGEMENTS

The report was prepared by Matthew Newman and Shawn Blosser on behalf of the City of Los Angeles Office of the Chief Legislative Analyst and the Office of Economic Analysis, which provided funding for the project. The analysis presented and the conclusions of this report are those of the authors.

EXECUTIVE SUMMARY

This report presents an assessment of the potential impact of a minimum wage for hotel workers in the City of Los Angeles (the City).¹

Minimum wage policies are generally intended to raise the wages of the lowest paid workers, and are frequently justified on the grounds that those working full time should not live in poverty. Beyond this basic argument, many have suggested that minimum wage policies can have other benefits, such as reducing income inequality and stimulating short-term economic growth. Others, however, have argued that increases in the minimum wage act to reduce employment among low-wage workers as employers look for ways to cut labor costs.

Assessing the likely impact of a minimum wage policy for Los Angeles hotel workers is complicated by the fact that most of the previous research on the topic has been conducted based on national or state level changes in the minimum wage, changes that effect low wage workers across industries. The effects of a local, single-industry minimum wage policy may well be quite different. Nevertheless, a careful review of the existing literature and an analysis of the economic factors likely to influence decisions made by employers and employees can point to some likely effects.

First, if a minimum wage for hotel workers were to be implemented, many workers would see a significant increase in their wages. These workers, in turn, would likely spend a fraction of these additional earnings in the City, thereby benefitting local firms and their workers. However, in response to the minimum wage increase, hotel profits would likely decline, and so too would the value of existing hotels; some hotel owners might be forced to sell or otherwise restructure their investments. Hotel owners would also seek ways to minimize the effects of a minimum wage increase, but most of the Los Angeles hotels subject to the new requirement would be limited in their ability to pass along any increased labor costs in the form of higher room rates. The result would therefore likely be reductions in staffing levels and reductions in certain purchases of goods and services in the local economy. Both of these effects would lead to reductions in economic activity which would at least partially offset any gains in economic activity generated by increased spending by those hotel workers who received a raise under the policy.

¹ Specifically, the City is considering a policy that would establish a minimum wage of \$15.37/hour for workers at hotels with 100 rooms or more and where workers are not subject to a collective bargaining agreement.

While the precise extent of these effects cannot be known with certainty, both existing research and established economic theory nevertheless suggest that such effects are likely. Therefore, establishing a minimum wage policy for hotel workers represents an inherent trade off. Newly hired or current hotel workers who remain employed would likely see a benefit, as would businesses that sell goods and services to these workers; however, these benefits would come at the expense of laid-off hotel workers or those not hired in the first place, as well as hotel owners who would see their profits decline.

This report was based on a review of research conducted by others and submitted to the City, comment letters received by the City with respect to the proposed policy, and a review of the published research literature relating to minimum wage policies more generally. This report does not reflect the results of any new empirical analysis of the issues at stake. Nevertheless, the available material provides a significant amount of research, data, and analysis which can be used by the City in assessing the likely impacts of such a policy.

INTRODUCTION

This report seeks to provide an assessment of the likely effects of a minimum wage for hotel workers in Los Angeles. Specifically, the City of Los Angeles is considering a policy that would establish a minimum wage of \$15.37 per hour for workers at hotels with 100 rooms or more and where workers are not subject to a collective bargaining agreement.²

In an effort to develop a more firm footing on which to assess the likely effects of such a minimum wage policy, the City engaged the services of the Office of Economic Analysis to review the materials submitted to the City by various stakeholders and others, and to conduct an analysis of the previously published research into the effects of minimum wage policies more generally. The issues addressed in these materials have been incorporated – to the extent relevant – into the analysis presented in this report. Specific comments about the three research reports submitted can be found in Appendix 1: Review of Economic Roundtable Reports. The questions and issues raised in the comment letters have been addressed, to the extent data and research were available, in the body of this report.

Impacts of Minimum Wage Policies Generally

Minimum wage policies are generally intended to raise the wages of the lowest paid workers, and are frequently justified on the grounds that those working full time should not live in poverty. Beyond this basic argument, many have suggested that minimum wage policies can have other benefits, such as reducing income inequality and stimulating short-term economic growth. This economic growth may occur because low income workers tend to spend much of their increased earnings in the local economy, thereby benefitting workers and employers at firms that supply goods and services to these workers. It has also been suggested that increases in the minimum wage can lead to other benefits for employers, such as reductions in absenteeism and turnover among affected employees.

These benefits notwithstanding, economists and business owners alike have suggested that increases in the minimum wage act to reduce employment among the low-wage workers these policies are intended to help. Whether and to what extent minimum wage policies in fact lead to job losses has long been a subject of debate among economists. Economic theory suggests that if wages are raised, employers will look for ways to cut labor costs by shifting more of the production process to capital equipment (e.g., by automating a process previously performed manually). Increases in the minimum

² According to the Economic Roundtable, 87 hotels in Los Angeles have 100 or more rooms. Of these 64 are not currently unionized and so would be affected by the new minimum wage policy. The current state minimum wage for California is set to rise to \$9.00 per hour on July 1, 2014.

wage may also act to increase worker productivity, which has the additional effect of reducing the number of workers or, alternatively, the number of work hours needed by employers. In addition to reducing employment, higher minimum wages may result in higher prices generally, leaving low-wage workers no better off in real terms. Finally, increases in the minimum wage may also reduce profits in affected firms, reducing the ability of and incentive for these firms to invest in expanding their businesses. Such increases could also encourage firms to relocate to other areas where wages are lower.

Because minimum wage laws are such a widely debated issue, a considerable amount of research into the effects of such policies has been conducted. Many of the economic effects of minimum wage policies can be expected to occur regardless of the jurisdiction and specifics of the policy at issue, and much of the research that has been conducted is therefore relevant to the proposal currently being considered by the City. However, many of the effects of a local policy such as the hotel worker minimum worker wage policy at issue in Los Angeles are unique to the specific proposal and jurisdiction in question. As a consequence, any effort to apply the existing research on minimum wages generally to the specific local policy in question must be careful to consider these unique circumstances.

Existing Research

The minimum wage has been the subject of research by economists for many decades. In fact, it has been claimed that “the minimum wage-employment debate... is as old as the Department of Labor.”³ Much of this research has focused either on specific industries that tend to employ more low-wage workers, such as fast-food restaurants or retail stores, or on teenagers or other populations most likely to be directly affected by minimum wage laws.

Economic theory suggests that, in a competitive labor market, increases in the minimum wage should lead to reductions in employment, either in the number of jobs or the number of hours worked. Many studies have supported this conclusion.⁴ For example, in their 2000 book *Minimum Wages*, economists David Neumark and William Wascher summarize the state of research existing at the time, concluding that “...the preponderance of evidence supports the view that minimum wages reduce the employment of low wage workers.”⁵ Neumark and Wascher also published a more recent review of the employment effects of the minimum wage in 2007. In this review they concluded that, “among the

³ Neumark, et.al. (2013), p.1.

⁴ See, for example, Brown (1999).

⁵ Quoted in Schmitt (2013), p. 4.

papers we view as providing the most credible evidence, almost all point to negative employment effects.”⁶

Although many studies have found a negative relationship between increases in the minimum wage and the number of jobs for low wage workers, the findings of some recent empirical studies have been less clear regarding the relationship between minimum wage increases and employment. For example, a 2013 study analyzed payroll data from a large, national retailer and found that the 1996 increase in the federal minimum wage resulted in no statistically significant change in overall employment at the firm.⁷ Similarly, a 2007 study analyzed the effects of San Francisco’s inflation-indexed local minimum wage, which raised the city’s minimum wage from the statewide level of \$6.75 to \$8.50 in 2004 and up to \$9.14 by 2007. That study, which examined the impact on both fast-food and table-service restaurants, found no statistically significant change in employment in San Francisco restaurants, both in terms of headcount and in terms of full-time equivalents (FTEs).⁸ Finally, in their recently published book, Dale Belman and Paul Wolfson provide a qualitative assessment of some 70 published articles on the impact of minimum wages on employment, as well as a meta-analysis using 439 distinct estimates of the effect of minimum wages from 23 of the studies reviewed. Based on this research, they conclude that “...if negative effects on employment are present, they are too small to be statistically detectable. Such effects would be too modest to have meaningful consequences in the dynamically changing labor markets of the United States.”⁹

If economic theory indicates that raising the minimum wage should result in lower levels of employment, why have some empirical studies found little or no measurable effect? A 2013 report by John Schmitt considers just this question. In addition to the potential problems that plague any empirical study, such as data shortcomings, the author identifies several possible ways that workers and employers may adjust to modest minimum wage increases other than simply reducing the number of employees.¹⁰ For example, employers might decrease the number of hours employees work, decrease non-wage benefits to these workers, or possibly reduce the salaries and benefits for higher

⁶ Neumark and Wascher (2006).

⁷ See Giuliano (2013).

⁸ See Dube et al (2007). Note that this study relied on survey data collected from San Francisco restaurants, and included the number of part-time and full-time employees (headcount) as well as the average weekly hours worked for each. They constructed their full-time equivalent employment measure as the total number of hours worked divided by 40.

⁹ See Belman, Dale, and Paul J. Wolfson. 2014. “The New Minimum Wage Research.” *Employment Research*. 21(2): 4-5. (http://research.upjohn.org/empl_research/vol21/iss2/2). The full book is available at <http://www.upjohninstitute.org/Publications/Titles/WhatDoesTheMinimumWageDo>.

¹⁰ See Schmitt (2013). As the author points out, these adjustment options were first enumerated by Barry Hirsch, Bruce Kaufman, and Tatyana Zelenska in their 2011 study entitled “Minimum Wage Channels of Adjustment” and published by the German Institute for the Study of Labor (http://www2.osu.edu/~ecobth/IZA_HKZ_MinWageCoA_dp6132.pdf).

paid employees in order to keep total labor costs in check, all of which could allow these firms to address the labor cost increase without reducing their total number of employees. Depending upon the competitive landscape, firms may also be able to raise their prices and pass along much of their increased labor costs to their customers or accept lower profits in response to increases in the minimum wage. The exact mix of responses could vary widely by region or by industry, or even among specific firms in the same industry. For modest increases in the minimum wage, the combined effect of all of these alternative responses could offset the negative effects of such an increase on the number of jobs for low-wage workers.

In spite of the fact that some published research has not shown a consistent and statistically meaningful effect from minimum wage policies on job losses, several recent studies have concluded that increases in the minimum wage can and do, under many circumstances, lead to reductions in jobs or the number of hours worked. For example, David Neumark and his colleagues revisited the minimum wage in a 2013 paper, concluding that, “the evidence still shows that minimum wages pose a tradeoff of higher wages for some against job losses for others, and that policymakers need to bear this tradeoff in mind when making decisions about increasing the minimum wage.”¹¹

Perhaps the most relevant analysis of how a proposed minimum wage increase might impact employment was recently published by the nonpartisan Congressional Budget Office (CBO) in February 2014.¹² This report assessed the potential impact of a proposal to increase the federal minimum wage from its current rate of \$7.25 per hour to either \$9.00 or \$10.10 per hour. The CBO conducted an extensive review of the published literature on the minimum wage, including both studies that found employment effects and studies that did not. Based on its extensive review of the existing literature, the CBO study concluded that (a) increases in the minimum wage can be expected to reduce (at least to some degree) the number of jobs for low wage workers and (b) a larger increase in the minimum wage will result in a greater reduction in employment. In addition, the CBO research concluded that, while an increase in the minimum wage would likely boost economic activity in the short term as a result of increased earnings on the part of low-wage workers, it would ultimately lead to reductions in economic activity in the long term, as the overall productivity of the economy declines due to reductions in the workforce.¹³

¹¹ Neumark, et.al. (2013).

¹² Congressional Budget Office (2014).

¹³ *ibid.*, p. 8.

Applying the Existing Research to the Current Proposal

Although the existing research on the effects of the minimum wage generally is extensive, the applicability of this research to the circumstances in Los Angeles is limited, at least to some extent.

First, most of the existing research has been conducted based on state or national changes in the minimum wage. When a single jurisdiction such as the City of Los Angeles adopts a minimum wage requirement that applies just to a subset of the firms in one industry, the effects of such a policy may be very different. For example, one of the effects of an increase in the minimum wage enacted across an entire state might be an increase in prices, allowing employers to pass along at least some portion of their increased costs. Because all firms face a similar increase in costs, affected firms may have the ability to raise prices without the risk that some competing firms will be able to leave prices low. If a single jurisdiction increases the minimum wage, however, competing firms located just across jurisdictional boundaries will not see an increase in costs. In such a circumstance, the ability of affected firms to raise prices without losing business to unaffected competitors is diminished (relative to the case in which all affected firms face higher costs). Because the proposal under consideration applies only to large hotels within Los Angeles, affected hotels likely would not be able to raise prices substantially in response to their increased wage costs.

Second, as the CBO concluded, larger increases in the minimum wage will likely lead to larger reductions in jobs or hours worked. Much of the previously published research examined relatively small increases in the minimum wage. The proposed increase in the minimum wage for hotel workers in Los Angeles, in contrast, represents a relatively large increase, at least for some classes of workers. Because this increase is larger than most of the increases that have been the subject of previous research, the relevance of this previous research is limited.

Third, as discussed above, most empirical studies that focus on specific industries have estimated the effect of a national or state minimum wage increase on businesses such as fast-food restaurants or retail stores. These types of businesses will certainly see their hourly wage costs rise, but they may also see demand for their products increase, as at least some portion of their clientele will be the beneficiaries of the minimum wage increase. Put another way, to the extent that low-wage workers earn more as a result of the increased minimum wage, they are likely to demand more goods and services, including those provided by fast food restaurants, retail outlets, and other establishments that employ low-wage workers. This enables such businesses to maintain or possibly even increase the number of employees or the total hours worked. The minimum wage increase proposed by the City of Los Angeles, however, applies only to hotels within the city limits, and the employees of Los Angeles hotels are not likely to also be the clientele for these hotels. Furthermore, when the minimum wage is increased on a statewide or national basis, there is much less potential for the effects of the policy to "leak" out of the affected region. In contrast, when the minimum wage is increased in a single

jurisdiction, many of the affected workers will spend their increased earnings on goods and services purchased outside of the local economy, thereby reducing the extent of any increase in economic activity stemming from these increased earnings. Therefore, while there could be some offsetting increases in low wage jobs in unaffected industries such as fast-food and retail, it is likely that either the number of jobs or the number of hours worked by hotel employees in Los Angeles would decline.

In spite of the limitations associated with applying the existing economic research to the case of a minimum wage increase for hotel workers in Los Angeles, we have attempted to utilize this research, combined with our review of research reports submitted by the Economic Roundtable, and a review of the comment letters submitted to the City to assess the likely effects of such a policy for the City of Los Angeles.

ECONOMIC EFFECTS OF RAISING THE MINIMUM WAGE FOR HOTEL WORKERS

Raising the minimum wage for hotel workers would likely result in a series of economic effects for the affected workers, their employers, and the City's economy. The precise extent and magnitude of these effects is not subject to reliable estimation, at least not with currently available data. However, the nature of the effects is more readily ascertainable. How then, might workers, employers, and the Los Angeles economy generally be affected?

Increased Wages

The first and most obvious effect of a minimum wage policy for hotel workers would of course be higher pay for these workers. Those hotel workers currently earning less than the proposed minimum wage of \$15.37 per hour would receive a wage increase to bring their pay up to the established minimum. In addition, some workers currently earning wages just below the new minimum might also get raises to levels above the new minimum in order to maintain an established wage hierarchy (e.g., more experienced employees currently earning \$14 per hour could see a raise to \$16 per hour in order to ensure that more experienced workers are paid more than less experienced workers). A similar result might occur with respect to some hotel workers currently earning in excess of \$15.37 per hour; some of these workers also would likely receive a raise in order to maintain a pay differential between staffing levels. For example a supervisor currently earning just above the \$15.37 minimum might also receive a raise in response to the required raise for supervised, lower-wage staff in order to maintain a pay differential between supervisors and those they supervise.

Reductions in Employment

As noted in the previous section, when faced with the increased labor costs associated with the proposed minimum wage increase, hotel owners or managers would have a number of options. One

likely result would be an effort to reduce the impact of the wage increase through reductions in staffing levels. Although the precise extent of any such reductions is not known, it is nevertheless likely that many hotels would reduce staffing levels and/or reduce the number of hours employees work. Evaluating the extent of these reductions is the subject of much of the published research on the minimum wage, but the most relevant and reliable studies have found that at least some level of staffing reductions is likely.¹⁴

These likely staffing reductions would result from several factors. By increasing the wages for workers, employers have the option to fill positions with more experienced, well-trained, and productive employees. These more productive workers would be able to do more work per shift or per hour relative to lower-paid and less productive workers, thereby reducing the need for workers overall. In addition, employers may increase workloads, in effect demanding that their employees work harder in exchange for the additional pay.

Some employers might also invest in labor saving technologies or other equipment that reduces the need for workers. For example, some hotels might invest in automated check-in kiosks in order to reduce the number of front desk personnel needed. Finally, some hotels would undoubtedly look to reduce staffing simply as a means of cutting costs, for example by eliminating or reducing the least profitable or popular hotel services.

Together, these factors would likely act to reduce, at least to some extent, the number of hotel industry jobs in the City or the number of hours worked by hotel workers relative to what would have been the case absent such a policy.

Reduced Profits

Another likely effect of the minimum wage policy would be a decline in hotel profits, at least for current hotel owners. For many if not all affected hotels, profits would decline in response to the cost increase represented by the higher minimum wage. This reduction in profits would in turn reduce the value of hotel properties. In some cases, the reduction in profits would simply mean reduced returns on existing investments. In others, however, it could force a hotel into bankruptcy or another form of financial restructuring. Such a bankruptcy, though it would represent a potentially significant financial loss for existing hotel owners, would not necessarily result in a hotel closure. Instead, it is likely that most such hotels would instead be sold – at a discounted price – to new owners. These new owners, facing lower

¹⁴ See especially Congressional Budget Office (2014).

financing costs as a result of the lower purchase price, could therefore more easily afford the higher wage costs required by the minimum wage policy and remain competitive.

Other Effects

In addition to these likely first order effects, several additional economic effects would potentially occur as well.

Increase in Local Economic Activity

As a result of the increase in wages paid to low wage workers, overall economic activity in the City would likely increase in the short term, although the extent of any such increase is unknown. That is, to the extent that the total take-home pay of Los Angeles hotel workers increases, these workers are likely to spend some portion of their increased earnings in the local economy, stimulating additional economic activity. Because a majority of these wage increases are likely to come from reduced profits or increased payments from hotel guests, this increase in economic activity would not be accompanied by an offsetting short term reduction in economic activity of a similar magnitude.¹⁵

If hotel owners find mechanisms to minimize the increase in overall payroll costs (for example by reducing staffing, hiring more productive workers, or increasing automation), the extent of any such increase in economic activity would be minimized, however. In the longer run, economic activity could be reduced if investment in new hotels is diminished or capital investments on the part of hotel owners are deferred (see below for a discussion of the likely effects on the incentive to invest in new hotels).

Impact on Room Rates

Many hotels would likely seek to raise their rates in response to the increased labor costs. And, for those hotels that are able to raise rates without suffering a significant loss in business, a portion of the costs of the proposed policy would be borne by visitors to the City.

However, the ability of many hotels to raise rates is limited. Hotels that primarily compete with smaller hotels (those with less than 100 rooms), hotels that are located near the City's boundaries and therefore compete directly with hotels in neighboring jurisdictions, or those that compete for regional or national convention business would be limited in their ability to raise rates.

¹⁵ Revenue from out of town visitors represents new money and therefore new economic activity from the standpoint of the City's economy. Revenue transferred from profits to employees would also largely represent new consumer spending in the local economy. And, while the reduction in profits might also be accompanied by a reduction in local consumer spending or a reduction in investment in the City, many hotel owners likely live, spend, and invest outside of the City of Los Angeles.

Hotels that primarily compete with other affected hotels for business travelers (e.g., downtown hotels) might have a greater ability to raise rates, although even hotels in this category would face competition from neighboring jurisdictions and from other cities for convention business and therefore would have a limited ability to raise rates.

Reductions in Local Spending by Hotels

Some hotels would also likely seek to address the increase in wage costs by reducing purchases of other goods and services, for example by delaying investments in facility upgrades or scheduled maintenance of hotel facilities. Hotels, like any profit maximizing business, already seek to keep costs as low as possible, so the extent of any such reductions is likely to be small. Nevertheless, some hotels would likely reduce some expenditures as a cost-saving measure. To the extent that these purchases of goods and services would have occurred in the local economy, a reduction in such purchases would result in a reduction in economic activity in the City, at least partially offsetting any increase in economic activity resulting from increased expenditures from hotel workers whose wages increase.

Impact on New Hotel Development

Any action that raises costs for an industry without providing simultaneous opportunities to increase revenues will lower profits. And, as an industry becomes less profitable, incentives to invest in that industry are diminished. To the extent that wage costs increase for Los Angeles hotels, but hotel owners cannot raise prices or cut other costs to offset these wage increases, hotels would become less profitable. This reduction in profitability would put downward pressure on new development, reducing the likelihood (at least to some extent) that new hotels would be developed in the City.

The extent of this effect, however, is mitigated by the fact that many potential new hotels would be, practically speaking, exempt from such a policy. Most new hotels built in the city in the past several years have received a subvention of transient occupancy tax (TOT) revenues as an incentive offered to developers to build in the City. As a condition for receiving the incentives, these hotels have agreed to enter into collective bargaining agreements with their employees. Because hotels with unionized workers are to be exempt from the minimum wage policy, any new hotel that receives a TOT subvention and agrees to hire workers subject to a collective bargaining agreement would not feel the effects of a minimum wage policy. Assuming this incentive continues to be offered going forward, the impact on future development of a minimum wage policy is diminished. Should the City discontinue the current development incentive policy, the disincentive for future development would be much greater. Similarly, to the extent that certain classes of hotels are not eligible for or do not seek the incentive, there would be a disincentive to develop such a hotel in the City.

Ultimately, the impact of a minimum wage policy on new hotel development would depend on whether and to what extent incentives offered to developers are sufficiently generous and broadly applied so as to mitigate the effects of lost hotel profits due to the minimum wage policy.

Disruptions for Low Wage Workers

Another potential effect of the proposed increase in the minimum wage is a disruption for many existing low wage workers. Because hotels would now be required to pay at least \$15.37 per hour to all of their workers, the lowest skilled workers (such as those currently earning well below \$15.37 per hour) would become relatively less attractive to employers. Instead, hotels would seek to hire the most qualified employee possible (for a given wage). Therefore, many hotels would likely seek to hire more experienced and productive workers, rather than continuing to employ or hire workers with more limited skills or experience.

CONCLUSION: INCREASE IN MINIMUM WAGE IMPLIES A TRADEOFF

While the precise extent of the economic effects discussed in this report cannot be known with certainty, both existing research and established economic theory nevertheless suggest that such effects are likely. Therefore, establishing a minimum wage policy for hotel workers – at least to a certain extent – represents an inherent trade off. Newly hired and current hotel workers who remain employed would likely see a benefit in the form of higher wages, as would businesses that sell goods and services to these workers; however, these benefits would come at the expense of laid-off hotel workers or those not hired in the first place, as well as hotel owners who would see their profits decline.

Features of the Proposed Minimum Wage to Consider

To the extent that the City chooses to adopt a minimum wage for hotel workers, several specific attributes of the policy are worthy of further consideration.

First, any such policy should be phased-in. The extent of the proposed increase in the minimum wage represents a relatively large increase for many classes of workers, and therefore represents a large increase in wage costs for employers. Allowing employers an opportunity to gradually adjust to the higher wage rates will help to minimize any adverse impacts or severe disruptions.

Second, an exemption for tipped employees should be considered.¹⁶ Many hotels workers who earn tips may already earn in excess of \$15.37 per hour. Therefore, requiring hotels to pay these tipped employees at the new, higher rate would have the effect of pushing the wages for these employees above the \$15.37 level. In addition, many tipped employees work in the food service area of affected hotels. Because hotel restaurants (and all food services to some extent) face competition from local restaurants not subject to the minimum wage policy, it is likely that such a policy would have a disproportionate effect on hotel restaurants and the workers at those restaurants.¹⁷

Possible Avenues for Additional Research

To a great extent, the impact of a minimum wage policy such as that currently being considered is simply not knowable beforehand. As discussed earlier in this report, a significant body of research has been conducted into the effects of such policies. Even with hindsight, careful students of this topic have not been able to achieve a clear consensus with respect to the effects of minimum wage policies that have already been enacted. In this context, the potential for research to conclusively demonstrate the likely future effects of a proposed policy is limited.

Nevertheless, one avenue of research in particular may be worth pursuing. During the past several years, minimum wage policies for hotel workers were adopted in both the City of Long Beach and the LAX hospitality zone. Both of these policies are similar in many respects to the policy currently being considered for the entire City of Los Angeles. Anecdotal evidence suggests that some hotels in Long Beach may have reduced staffing levels in response to the minimum wage policy. However, we are not aware of any research or analysis that has been published which conclusively demonstrates (one way or the other) the impact of the Long Beach minimum wage policy on employment. The minimum wage policy for hotel workers in the LAX hospitality zone was the subject of a study by the Economic Roundtable. However, as noted in the Appendix to this report, this study does not provide a sufficient basis with which to judge the effects of the policy on hotel employment. Therefore, a study aimed at assessing the effects of these two minimum wage policies could help to shed some light on the limited question of what effects such policies might have on employment in the Los Angeles hotel industry. Addressing the broader question of the overall economic effects of such policies, including any short-term increase in economic activity and any long-run decrease in hotel development would be more complicated to analyze.

¹⁶ Currently, the federal minimum wage law allows for a separate, lower minimum wage for tipped employees. However, California's minimum wage law offers no such exception. Therefore, any potential legal issues associated with excluding tipped employees would need to be addressed if such an exemption were to be considered.

¹⁷ Note that legal and practical limitations may restrict, at least to some extent, the ability of the City to exempt tipped employees. This issue should be explored with the City Attorney.

APPENDIX 1: REVIEW OF ECONOMIC ROUNDTABLE REPORTS

The Economic Roundtable submitted three research reports to the City in response to a request for relevant research or information about the effects of the proposed hotel worker minimum wage policy.

The first of these reports, entitled “From the Pockets of Strangers,” dates to 2006. This report describes the relative size and character of the City’s tourism economy, identifies the benefits of tourism, and presents some recommendations for actions that could be taken to boost the tourism economy. While this report contains some useful information, the material, now more than eight years old, combined with a focus not directly relevant to the subject of the current minimum wage debate limits the relevance and usefulness of this report for purposes of evaluating the likely impacts of a minimum wage for hotel workers.

The second Economic Roundtable report, prepared in 2010 and entitled, “Impacts of Living Wages in the Airport Hospitality Enhancement Zone” is more directly on point with respect to helping to identify the likely effects of a minimum wage for hotel workers. However, two factors act to limit the usefulness of this report for the current purpose.

First, the report was prepared in December 2010, just a couple of years after the airport hospitality zone polices went into effect, and many of the economic impacts from such a policy can take years or longer to emerge. In addition, the policy was implemented in 2008 during a period of significant economic disruption brought about by the “great recession,” making it difficult to separate out the effects of the policy from the economic conditions at the time. For these reasons, any conclusions about the impact of such a policy coming so soon after the policy’s implementation must be considered preliminary.

Second, and more importantly, the methodology used to analyze employment changes at affected hotels is too imprecise to allow for useful conclusions to be drawn. The conclusion of the report, namely that “living wage standards... have had positive, or at least not negative, impacts on hotels, hotel customers and hotel workers” relies primarily on changes in employment reported by survey respondents living close to or in the airport hospitality zone as compared to responses of those living elsewhere in the City. However, this approach is subject to two important limitations. First, the sample sizes used for many of the survey responses are quite small, with correspondingly large confidence intervals. This means that that the actual responses from the entire population of hotel workers could be quite different from the results reported by the relatively small number of workers who responded to the survey. Second, the conclusions rely on the assumption that the hospitality zone workers also live in the hospitality zone, while the non-hospitality zone workers do not live in the hospitality zone. In a City as mobile as Los Angeles, in which many commuters travel long distances (many from outside of the City or even the County) to work, this assumption would require stronger support than what is provided in the report if the report’s conclusions were to be relied upon.

In spite of these limitations, neither the age of the data nor the limitations in the methodology employed suggests that the conclusions presented are incorrect. In fact, it may well be the case that the conclusions presented are true. However, the material presented in the report does not provide a sufficient basis for drawing such conclusions.

The third Economic Roundtable report entitled "Repaying Hospitality" is directly aimed at the topic at hand. This 2013 report aims to address the question of what would be the economic effects of a minimum wage policy for hotel workers in Los Angeles. The report reaches two important, relevant conclusions. First, the report suggests that "a new minimum wage will not result in significant relocation or cessation of current hotel business."¹⁸ Second, the report suggests that a hotel minimum wage policy would increase local economic activity as a result of the increased consumer spending on behalf of hotel workers.

As evidence to support the first conclusion with respect to hotel closures, the report cites the example of the airport hospitality zone, which, despite a minimum wage policy adopted in 2008, has not seen any hotel closures in the intervening period. The report also suggests that the relative strength of the Los Angeles hotel sector (with rising occupancy rates) and the fact that many hotels have existing customers loyal to the brand or individual property further suggest that closures are unlikely. While any assessment of the likelihood of hotel closures would be to some extent speculative, this conclusion nevertheless seems reasonable. As discussed in the body of this report, it is likely that a minimum wage policy would reduce the value of affected hotel properties. However, this does not necessarily mean that hotels would close as a result. Instead, some hotel owners may be forced to sell their properties to new owners. These new owners, facing lower financing costs as a result of the reduced purchase price, would therefore be able to afford to pay higher wages as required by the proposed minimum wage policy and still make a profit. It is certainly possible that some hotel owners would choose to convert their properties to alternative uses rather than continue to operate these properties as hotels. However, changes in hotel ownership are not uncommon, and therefore the most likely conclusion, as indicated by the Economic Roundtable, is that few if any hotels would close down and cease operating as a result of the minimum wage policy.

The report's second conclusion, that local economic activity would increase, is also supported by the available evidence. However, the magnitude of the expected increase presented in the study likely overstates the extent of the effect. First, the estimated increase in economic activity is based on the assumption that all workers currently earning less than the proposed minimum wage would get a raise

¹⁸ Burns, Patrick, "Repaying Hospitality." Economic Roundtable 2013, p. 1.

to \$15.37 per hour. However, as noted in the body of this report, it is likely that, owing to increases in worker productivity and other factors, the number of workers in the Los Angeles hotel industry would decrease. To the extent that the number of affected workers is smaller, the size of the economic increase would be smaller as well. Second, as pointed out in the body of the Economic Roundtable report, the estimated economic impact does not reflect the likelihood that many hotels would seek to offset their higher wage costs by reducing purchases of other goods and services from the local economy. If local purchases are reduced, this would cause an offsetting reduction in economic activity. Similarly, because a fraction of hotel revenues comes from local residents (the report suggests that approximately one-quarter of revenues are from local customers), these residents would face higher costs to the extent that prices are increased. Therefore, any price increases passed on to local residents would cause an offsetting reduction in local economic activity, since these residents would have less to spend on other local goods and services. Therefore, the figure reported by the economic roundtable likely overstates the size of any increase in economic activity.

Finally, the report makes no effort to adjust the reported total economic benefit for the possibility that future hotel development could be curtailed. Estimating any such change is admittedly challenging and even speculative. Indeed, as the body of this report points out, any decreases in future development could be mitigated by the City's current practice of offering developers a subvention of transient occupancy tax revenues as an incentive to develop new hotels within the City. However, it is likely that at least some reduction in future development would nevertheless occur. Such a reduction in future development would result in reductions in economic activity relative to the level that would have occurred absent a minimum wage policy.

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