Evaluating the Impact of Federal Legislation on Small Businesses: An Exploratory Study of the New Minimum Wage Rate and the Health Insurance Tax

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Abstract

In 2010, Congress passed a Health Care bill that was widely criticized due to concerns of the impact it would have on small businesses. The proposed legislation originally included a provision to charge an insurance premium tax for firms with payrolls greater than $250,000. The final version of the bill greatly modified the provisions that would have charged an insurance tax to small firms with over fifty employees. This study evaluates the impact on labor costs of the proposed health insurance tax as well as recent increases in the minimum wage rate. We address the health insurance tax provisions because Congress has suggested new provisions may reduce the fifty-employee threshold.

We offer a discursive assessment of the impact of the federal legislation with regard to minimum wage and the proposed health insurance surcharge on small businesses with $250,000 in labor costs that do not carry health insurance for their employees. We use a modified case study to evaluate the financial impact of federal legislation on a typical firm in the restaurant industry. This industry is particularly important because it contains small businesses with many employees earning minimum wage and working part-time.

The paper concludes that a firm with as few as 20 employees would have as much as a 50-55 percent decrease in net income as a result of the two federal labor laws discussed in this research. The costs identified in this study are not insignificant because they may become a reality for firms with fewer than 50 employees if the bill is modified. The change in the minimum wage law alone can have a severe impact on the labor costs and net income of a small firm for companies with as few as 5 employees.

Introduction

External laws and regulations can have a serious impact on small business performance (Robinson, et al, 1998). Wage rates and the taxes on those wages affect the total labor costs incurred by all businesses. Small firms are especially challenged by changes in their labor costs because the burden is often not shared by multiple shareholders, but rather by a sole proprietor or a few shareholders in a closely held firm. On July 24, 2009, the national minimum wage increased by $0.70 per hour for all employees. In 2009, Congress proposed new health insurance legislation that would charge an eight percent premium to firms with total labor costs exceeding $250,000 if those businesses did not provide health insurance for their employees.
When it was originally proposed, the Health Care Bill was questioned by a variety of individuals and organizations. Following a great deal of debate, the provisions that would charge an eight percent premium to firms without health insurance were eliminated from the bill, except for firms with over 50 employees (We use the term “Health Care Bill” for simplicity). Yet, one can’t help but wonder just how much effect this health insurance premium would have had on small firms. What kind of impact might this provision of the bill have had on a small business or its owner? Was it reasonable for Congress to ignore societal concerns that small firms do not provide health insurance coverage to their employees (Kaiser/ HRET, 2009)? This question is not merely academic because the House of Representatives is also considering amendments to the bill that could impose a burden on small firms that are not presently in the version of the bill passed by both the House and the Senate (deMause, 2010). For example, one possible change would count part-time employees toward the 50-employee minimum (deMause, 2010).

Thus, the purpose of this paper is assess the impact changes in minimum wage as well as the proposed changes the health insurance premium would have on small businesses. These issues are not trivial. They can be especially significant to entrepreneurs and small business owners for four reasons. First, while the U.S. Small Business Administration notes that the vast majority of firms have fewer than fifty employees, there are at least 216,760 that have between fifty-one and five hundred employees (Small Business Administration, 2009a). Second, small businesses generally do not have human resource expertise in place to manage the impact of such changes. Third, an increase in labor costs will have a direct impact on the net income of a small business, many of which are operated as sole proprietorships or closely owned business
entities. Lastly, the health care bill that was passed in March 21, 2010 is subject to amendments that may further impact small firms with fewer than 50 full-time employees (deMause, 2010).

**Background Literature**

Numerous articles advise a small business owner about how to handle everything from AIDS in the workplace (Franklin and Gresham, 1992; Hoffman and Clinebell, 2000) to sexual harassment (Robinson, et. al. 1998) and taxes. Compliance with tax regulations, environmental regulations, employment regulations, accessibility regulations, industrial and safety regulations, and the impact of federal laws on business are just a few of the myriad of legal topics addressed by the literature. When examining industry-specific topics, the review of specialized standards for performance and operations, quality and control, and industry-wide guidelines may also be determinative of how a firm channels its legal resources. Other opportunities for detailed review of legal concerns include the ownership of land and facilities and the impact of the locality on zoning and planning regulations that affect the business.

Nonetheless, both the human resource literature and the small business literature is largely mute about minimum wage and the proposed new health insurance tax on small businesses with $250,000 in labor costs that do not carry health insurance for their employees. Of course, these two issues are literally new topics for analysis and discussion. The new minimum wage rate went into effect on July 24, 2009. Most of the provisions of the Health Care Bill will not go into effect for approximately 12-18 months.

In the next section we discuss both the minimum wage and the proposed new health insurance tax on labor costs above $250,000. In the third section, we evaluate the impact of
these two increases in labor costs on both the small business owner’s perspective using financial analysis. In the fourth section, we address the potential response a small business owner may have to these two changes. In the final section, we suggest possible directions for future research.

**Minimum Wage**

In 1938, the Fair Labor Standards Act was passed, which was a sweeping piece of employment-related legislation. One provision of this act was the creation of a “minimum wage”. This wage was originally set at $0.25 an hour. Over the years, the U.S. government has increased this amount, most recently from $6.55 an hour to $7.25 an hour, the third consecutive annual increase. As recently as June 30th, 2007 the minimum wage was $5.15 an hour. On July 1, 2007, it was increased to $5.85 an hour, a 13.6 percent increase. The following year, it was increased to $6.55, a 12 percent increase and then most recently to $7.25, and increase of 10.7 percent. The total jump of $2.10 an hour over the 2 year period is a 40.8 percent increase in minimum wages (US DOL, 2009). Such a large increase in minimum wage sparks concerns about the potential to decrease demand for minimum wage labor, particularly in an environment of rising unemployment and economic distress. Several recent analyses of the relationship between minimum wage rates and unemployment find a positive relationship between minimum wage rates and unemployment, particularly among small businesses, retail employment and most strikingly among teenage workers, the largest pool of minimum wage workers (Neumark and Wascher, 2009; and Sabia, 2006). A 2009 study by David Neumark of the National Bureau of Economic Research and William Wascher, a member of the Board of Governors of the Federal Reserve System - Division of Research and Statistics, reviewed the
past studies examining minimum wage and unemployment. They found that increases in minimum wages consistently caused declines in employment, particularly among the least skilled workers. A 2006 study by Joseph Sabia sheds further light on this relationship. His study looked specifically at employment in the retail and small business sectors. He found that increases in minimum wage fairly consistently related to decreases in employment in those sectors. Specifically, he found that a 10 percent increase in minimum wage translated to approximately a 1 percent decline in employment in the retail and small business sectors. Using his numbers, the recent 40 percent increase in US minimum wage would be expected to have a 4 percent disemployment effect on workers in retail and small businesses. He also found that this effect was amplified for low-skilled employees. Teenaged workers were the most affected by such a change. Specifically he found, “A 10 percent increase in the minimum wage is associated with a 2.7 to 4.3 percent decline in teen employment in the retail sector, a 5 percent decline in average retail hours worked by all teenagers, and a 2.8 percent decline in retail hours worked by teenagers who remain employed in retail jobs” (Sabia, 2006, p. 5). This would contribute to recent reports that the unemployment rate for black teenage males is fifty percent and the rate for white teenage males is 26.5 percent (Bartlett, 2009). Furthermore, Bartlett cites Bureau of Labor Statistics data that indicate that, “Well over half of those paid at the minimum wage are under the age of 24 and two-thirds of them are teenagers. Almost 60 percent work part-time and more than half work in food preparation and serving-related occupations. Minimum wage workers are not well educated. About 40 percent don't have a high school diploma, and a third have only a high school education. Just 3 percent of those working at the minimum wage have graduated from college.” He also points out that among
the US workforce of 155 million, only 95 thousand work full time at minimum wage in 2008. In short, the impact of the minimum wage increase was largely upon part-time, teenaged workers, not the elusive starving family surviving on minimum wage.

Health Insurance

Before we can understand the implications of health insurance for small businesses, we must first understand the health care system in the U.S. In a monograph prepared by Louis Rossiter, he makes the following statement, based upon his analysis of the place healthcare has within our overall economy:

The basic problem is not simply that we are spending more on healthcare in terms of how much we use and the price of that care. The problem is the accelerated rate of the increase when compared to other components of the economy. As each year passes, healthcare consumes an ever-larger share of expenditures, increasing from 9.4 percent in 1981 to 16 percent in 2006. Today, that figure is higher (Rossiter, 2009, p. 4).

Health insurance among small businesses is an important issue. According to a research study by the National Federation of Independent Businesses (Phillips and Wade, 2008), the rising costs of health insurance are the number one problem faced by small business owners. Their study of 3,530 small business owners in 2008 identified problems and priorities the business owners believed to be the most critical to them from among a list of 75 potential items. Health insurance was identified as the number one small business problem for the twentieth consecutive year that this series of research studies has been conducted. The magnitude of this particular problem is quite alarming. Fifty six percent of the respondents of this study indicated it was a “critical’ problem while the second most cited problem, “Energy Costs, Except Electricity,” was rated critical by only fourteen percent of the respondents.
The issue of health insurance has reached extreme levels according to some studies. According to research conducted annually by the Henry J. Kaiser Family Foundation between 1999 – 2009, the percentage of firms offering health benefits has declined from 69 percent in 2000 to 59 percent in 2009 (Kaiser/ HRET, 2009). As one might expect, their research also found “The smallest firms are least likely to offer health insurance. Only forty-six percent of firms with 3 to 9 workers offer coverage, compared to 72 percent of firms with 10 to 24 workers, 87 percent of firms with 25 to 49 workers and over 95 percent of firms with 50 or more employees” (Kaiser/ HRET, 2009, p. 34). Figure 1 shows the data from the 2009 Kaiser/HRET study. Costs were cited as the primary reason in the 2009 Kaiser/ HRET survey by 41 percent of the firms that did not offer health insurance.

Figure 1. Percentage of Firms Offering Health Benefits, by Firm Size, 1999 – 2009

<table>
<thead>
<tr>
<th>Firm Size (Workers)</th>
<th>1999</th>
<th>2000</th>
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<tr>
<td>3 – 9</td>
<td>56%</td>
<td>57%</td>
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<td>52%</td>
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<td>10 – 24</td>
<td>74%</td>
<td>80%</td>
<td>77%</td>
<td>70%</td>
<td>74%</td>
<td>72%</td>
<td>73%</td>
<td>76%</td>
<td>78%</td>
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<td>25 – 49</td>
<td>86%</td>
<td>91%</td>
<td>90%</td>
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<td>50 – 199</td>
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<tr>
<td>All Small Firms (3 – 199)</td>
<td>65%</td>
<td>68%</td>
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<td>66%</td>
<td>65%</td>
<td>63%</td>
<td>59%</td>
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<td>59%</td>
<td>62%</td>
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<td>All Large Firms (200 or more)</td>
<td>99%</td>
<td>99%</td>
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<td>ALL FIRMS</td>
<td>66%</td>
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* Estimate is statistically different from estimate for the previous year shown (p<.05).
The academic literature on health insurance and small businesses is limited at best. Some of the topics in the literature include studies that confirm the extent of health insurance coverage among small firms (Robinson, 2008), recommendations regarding managed care (Bradley and Hobbs, 2008), the perceptions of small business owners of the cost of health insurance, and several studies about the costs of health insurance (Robinson, 2008; Opiela, 2008). This last issue is the primary topic in the academic literature when health insurance has been covered. These studies reach the same conclusion: the cost of health insurance is prohibitive for small firms (Opiela, 2008; Kathawal, Elmuti & Roszkowski, 1993; and Morrisey, 2003). Small firms are simply not able to negotiate health insurance contracts (Cebula, Gubenko, & McGrath, 2007). Benoit points out that rising health care costs explains why employers are “choosing looser managed care products in response to the managed care backlash…” (Benoit et al., 2007, p. 66). In a Government Accounting Office (GAO) study, Allen (2001) finds that small firms tended to have higher average cost-sharing requirements and did not offer certain benefits such as psychiatric and chiropractic coverage (Allen, 2001). Yet, it is hard to gauge the magnitude of health insurance costs in small firms because the literature provides absolute values among a sample of firms (see, for example, Kaiser/ HRET, 2009). Survey research has been used previously, but it has not captured the relative magnitude of health insurance, especially relative to other expenses of a profitably operating small business. Thus, before public policy on health insurance can be properly enacted, government policy makers must understand the relative magnitude of these costs. It is this gap in the extant literature that we address in this study.
Research Method

This study employs a modified case study to evaluate the affect of the new minimum wage standard and proposed health insurance tax on small firms. The challenge of conducting research about these two subjects and small businesses is that the literature on either subject is rather limited. Thus, a more traditional empirical study would not be appropriate. The emphasis in this study is on the affects of the new minimum wage and health insurance tax at the firm level which does not lend itself to survey methodology. Hence, we employed a more exploratory stage of research (Gorman and Hanlon, 1997). In such a situation, it is appropriate to use a qualitative research method in order to gather the necessary information (Eisenhardt, 1989; Yin, 1994). The current research necessitated that we observe the affects of the new minimum wage standard and the proposed health insurance tax on the financial performance of a single small business. Thus, we adopted a qualitative research method described by Audet and d’Amboise (1998) in their study which was broad-minded and flexible. Like their study, our aim was “to combine rigor, flexibility and structure without unduly restricting our research endeavor” (Audet and d’Amboise, 1998, p. 11 of 24).

In order to focus on the financial impact at the firm level, we first look at minimum wage and health insurance for firms ranging in employment size of five or fewer employees to firms with as many as forty employees. These numbers of employees are consistent with what we know from the Kaiser/ HRET series of studies. Next, we use the financial statement from a single firm with a high percentage of minimum wage workers to assess the impact of the new minimum wage rate, with adjustments for firm size. Finally, we summarize these affects to gain
a perspective on the overall impact of the new minimum wage standard and proposed health insurance tax on the financial performance of a small business.

**Labor Costs**

We evaluate the cost of raising the minimum wage rate to $7.25 for small businesses based upon sizes of 5 employees, 10 employees, 20 employees, and 40 employees. Our evaluation holds other factors constant. Table 1 shows our findings.

Since many minimum wage earners work part-time (DOL, 2009a), which can vary from 1 – 34 hours (DOL, 2009b), we used 25 hours as a base number of hours.

**Health Insurance Tax Costs**

The bill will charge small businesses with more than 50 employees a penalty of 8 percent per employee. According to the Small Business Administration, approximately 284,286 firms have between 50 and 500 employees (SBA, 2009c). Thus, it would not appear that many very small firms will be affected. However, this conclusion may be spurious. As noted earlier, provisions may count part-time employees on a pro-rated basis toward the 50-employee minimum (deMause, 2010). Thus, smaller firms could easily be impacted. For example, a company with 40 full-time employees and 20 part-time workers could be counted as a firm with 50 full-time employees. Should the bill be more costly than anticipated, then even more modifications may be made in order to cover the increased expenses. Hence, we maintain it is a valuable process to consider the impact of health insurance penalties on firms with fewer than 50 employees.
As the literature review points out, discussions of health insurance for employees of small business is very recent. More importantly, the literature that does address health insurance focuses on a macro-economic perspective. We choose to consider the implications of this proposed legislation solely on the financial performance of a typical small business with employees. Table 2 shows our calculations for firms differing in size by employment, starting at 5 employees and increasing to 10 employees, 20 employees, and lastly, to 40 employees. Each of these levels of employment are consistent with the criteria used to define a small business in the United States (Small Business Administration, 2009b).

**Total Change in Costs to the Small Business**

To this point, our analysis has separately addressed the impact of the new minimum wage rate and the proposed health insurance tax. We now combine these two analyses to determine the total change in payroll costs to the small business. For this study we selected a relatively small, publicly traded, food service business. Food service businesses commonly employ a high percentage of part-time, minimum wage employees (DOL, 2009). Buffalo Wild Wings, Inc. went public in 2003, operates 197 restaurants and has 363 franchise units. The company has 12,000 employees; 1,000 full-time, 10,800 part-time and 200 employees based in the home office or field support management positions. Assuming all part-time employees work in the restaurant operations, there are approximately 55 part-time employees per restaurant. The corporation’s 2008 Consolidated Earnings Statement is presented in Table 4 (from the company’s 10-K report).

We wanted to analyze the effects of the current change in minimum wage and proposed health insurance tax on a single restaurant. The consolidated financial statement numbers
were divided by 197 restaurants to approximate the earnings of a single restaurant. Ideally the franchise royalties and fees and related general and administrative costs and expenses would have been eliminated from the analysis to better isolate the restaurant activity. The franchise royalties and fees are easily identifiable; however, the portion of general and administrative costs and expenses related to the royalties cannot be determined from the information provided in the corporation’s 10-K report. Therefore, we did not eliminate the revenue or the related expenses from the analysis.

As noted, part-time employment is defined as working between 1 and 34 hours per week. For this analysis we used 25 hours per week as the average part-time employment. In order to estimate the effect of the increase in minimum wage, we used 25 hours, 55 employees, for 50 weeks, times the seventy cent increase in minimum wage, plus the increase in social security tax on this incremental increase at the 7.65% rate. The effect of the eight percent insurance increase was computed on the total estimated part-time payroll using the new minimum wage. Buffalo Wild Wings is currently self-insured. We applied the eight percent increase in labor costs only to the part-time employment because the originally reported earnings statement would have included an insurance cost for full-time employees.

The results reveal that the effects of the minimum wage and insurance tax are not immaterial. The combination of these two changes decreases net income by approximately one-half. Net income decreases from 5.3 percent to 2.4 percent. When comparing the return on investment from running this successful restaurant to the return from investing in a treasury bond, the restaurant becomes even less appealing financially.
Taking the analysis for the change in the unemployment rate and the proposed health insurance tax into account we gain an appreciation for the total change in costs to the small business. We used the financial statements of the Buffalo Wild Wings, Inc. restaurant chain for this step. We chose this restaurant for two reasons. First, the Department of Labor maintains records of employment across all sectors of the economy. The restaurant industry has the highest percentage of workers that are paid minimum wage. Thus, a firm in this industry serves as a reasonable basis for analysis of changes in minimum wage. Secondly, we were reasonably confident in the reliability and external validity of Buffalo Wild Wings, Inc.’s financial statements. A perusal of Yahoo!® Finance provided a list of sixty-two companies in the restaurant industry with summary financial ratios for each of them which included Buffalo Wild Wings, Inc. Their profit margin of 5.3 percent was similar to the 7.7 percent profit margin for all firms in the Yahoo! Finance database.

Discussion

This study employed a modified case study method to evaluate the impact of the new minimum wage standard and proposed health insurance tax on the financial performance of a small business. Previous research focused attention on the macro-economic impact changes in minimum wage have on the American economy. Similarly, research on health insurance has focused on the absolute costs to the small firms or the macroeconomic impact changes to our system would have on the country. This study asked the simple question, “To what extent do these two factors affect the financial performance of a small business?” Our goal was to observe the relative magnitude of these factors on the financial performance of a single small
business. Since the original analysis of this issue, Congress has modified the bill that was proposed and passed legislation that does not impose the 8 percent tax premium on employers with smaller than 50 employees. However, members of Congress have indicated the Health Care Bill is not complete (deMause, 2010). Additional modifications are likely such as small business provisions that begin to count part-time employees against the 50-employee minimum on a pro-rated basis (deMause, 2010). This type of change can be instituted through the reconciliation process (Rovner, 2010) which only requires a majority vote. Barnes (2010) points out that forecasts of the cost of the Health Care Bill have been underestimated. More importantly, if the Medicare Act is a predictor of the Health Care Bill, then it will cost considerably more. More recently, the Congressional Budget Office indicated the new bill would cost $115 billion more than originally forecasted (Tapper, 2010). Clearly, if the bill costs more than planned, Congress will have to pay for it in some way.

As part of our research design, we selected a relatively small, publicly traded, food service business. Food service businesses commonly employ a high percentage of part-time, minimum wage employees (DOL, 2009). In addition, depending upon employment figures, they may be impacted by the proposed health insurance legislation. Thirdly, this particular restaurant chain reported net earnings that were near the mean of a sample of 62 similar companies evaluated by Yahoo! Finance. The results of our financial analysis reveal that the effects of the minimum wage and insurance tax are material. The combination of these two changes decreases net income for a single franchisee restaurant by approximately one-half. Net income decreases from 5.3 percent to 2.4 percent.
Implications for Future Research and Small Businesses

In this section we address the implications for future research as well as the practical implications for small businesses. It is clear that the change in the minimum wage rate will have a profound effect on the labor costs of many small firms. The Health Care Bill will only have an effect if the legislation is modified to lower the 50-employee threshold. This study addresses just such a scenario. When both health insurance tax and the new minimum wage rate are taken into account, their impact is rather startling. In our example, the restaurant’s profit margin falls by a factor of one-half from 5.3 percent to 2.4 percent, solely due to the impact on labor costs.

Such a drastic change in the financial position of a company could not be ignored. Faced with such a drastic decline in profit margin, a small business owner has some options available to them. Some of these options are rather predictable, while other options are plausible, but less predictable. Thus, we consider how a small business owner may respond to increases in their cost of labor due to the new minimum wage rate and/or the proposed health insurance tax.

One option available to the owner is rather predictable. According to studies by Morrow, Johnson, and Busenitz (2004) and Pearce and Robbins (1994), the typical response by companies faced by this type of situation is to seek cost-cutting measures, which typically include layoffs. Thus, one possible outcome is that small firms faced with increases in minimum wage and health insurance penalties would layoff employees. In fact, the literature on minimum wage earners points out an increase in the minimum wage has a negative
employment effect among teenagers and low-skilled workers (Neumark and Wascher, 2007). It remains an empirical question whether small firms would layoff workers

A second option we might label “1B” as a small business may layoff workers solely due to the health insurance penalty. While the minimum wage law may not raise wages on their existing employees, the new health insurance penalty may impact a firm. Table 4 shows how few full-time workers are required for a firm to reach $250,000 in annual payroll costs. Consider a firm with payroll of $250,286.25 as shown in Table 4, based upon a mix of eight full-time employees and eight part-time employees. Congress is still debating the fine details of the proposed legislation, but cutting hours for a worker or simply laying off an employee will lower payroll below the ‘magical’ threshold of the current legislation proposed in Congress.

Another variation of this option would be to manipulate the ownership of the organization. A closely held firm with multiple locations could simply spin off the locations as separate companies. So long as a holding company is not involved this option may be rather novel, effective yet unethical.

A third option is the traditional human resources choice of capital vs. labor. In a situation of escalating labor costs, businesses frequently opt for the choice of buying machinery that makes labor unnecessary. Both the increase in the minimum wage and the proposed health insurance tax will raise the labor costs for many small businesses. In this case, the dual jeopardy introduced by an increase in the minimum wage accompanied by a forced insurance program is a significant enough change to the cost of labor to greatly impact the labor versus capital decision. Companies that were comfortable with a labor intensive manual process may be willing to invest in significant capital equipment that would have previously been cost
prohibitive. As is always the case, a business owner must choose the option that provides the customer with the best product or service at the lowest cost. If it becomes cheaper to purchase a mechanized process to complete the product or service, companies will have no choice but to accede to the economic reality.

A fourth option a small business owner may make is to relocate their labor intensive processes outside the US. For the past several decades, US businesses have found themselves in the unfortunate and uncomfortable position of having to close US plants to relocate the manufacturing or services to a location in a low labor cost location. Locations such as China, India, Korea and Mexico are often chosen due to low labor costs (Longenecker, et al., 2008) and less restrictive legal requirements.

Mark Wilson (2009) argues that in response to an 8% health insurance penalty, some small firms may drop coverage for their employees. Why would they do so? Quite simply these small business owners would do so if the product of eight percent times their payroll expense is less than the amount they presently pay in premiums for the employee’s health coverage. The Bureau of Labor Statistics reports that the average cost of health insurance to a business is 11.6 percent of wages and salaries which is clearly higher than the proposed tax of 8% (2009). The Congressional Budget Office (CBO, 2009) points out a flaw in this portion of the proposed legislation is that employees that have their employer-sponsored health insurance dropped would then have to look elsewhere for health insurance as the 8 percent penalty has not been directed to make a contribution to the employee’s insurance costs.

A final option related to health insurance costs that may be considered by the small business owner has been addressed in previous studies discussed in this research. Allen (2001)
pointed out that some small firms simply reduce the benefits to their employees as their portion of the insurance premium rises from year-to-year. Thus, the company would continue to offer health insurance to its employees, but the scope of that coverage would shrink. The employees would receive fewer services for what would most likely be a higher premium as health care costs rise (Rossiter, 2009; Kaiser/HRET, 2009).

We cannot say with certainty that a small firm will choose any of the aforementioned courses of action. Yet, any of these courses of action is plausible. Some of them, such as layoffs or reduced benefits for health insurance, have been identified in the literature. Thus, we can be relatively confident that some small businesses will choose those alternatives. In the event they do, then the very people these government policies are intended to benefit may very well be harmed.

The findings of this study demonstrate the possible unintended consequences of well intentioned government policies. The intent behind minimum wage is to provide a “decent” wage for working Americans. Similarly, the proposed health insurance legislation is noble because it attempts to address the gap (Rossiter, 2009) between the number of Americans that are insured versus those that are not. Most people would agree that one role of government is to care for its citizens. However, we demonstrate that several possible outcomes may occur, depending upon the individual choices small business owners make as minimum wage rates and health insurance tax evolve over the next several months, that are simply not beneficial for employees.

Small businesses frequently begin with little net income. The restaurant business in our study is small for a publicly traded business. The estimated effects of the increase in minimum
Wage and insurance tax cuts net income to just over two percent. As an investor exploring new business and investment possibilities, one must question whether this return is enough to encourage investment in small business. Investors can earn similar returns or better with a bond fund with little to no risk.

At the same time, banks have tightened credit lines and are less willing to lend money. So the increase in minimum wage and insurance tax may add to the credit crisis, by further decreasing the investment capital available for new startup businesses and small businesses.

More importantly, a decrease of net income to two percent may force drastic a reaction by the owner(s). Cost cutting measures will likely occur. These measures generally involve manipulation of labor costs (Morrow, Johnson, and Busenitz, 2004; Pearce and Robbins, 1994; and Allen, 2001) which would not bode well for the firm’s employees.

The recent change in the minimum wage provides new opportunities to explore the relationship between a change in minimum wage and employment in the US that can further improve our understanding of this important issue. It represents a natural experiment that can contrast the impact in states without a state level minimum wage with states that have a state mandated minimum wage that is higher than the federal rate.

Yet, a macroeconomic view of national unemployment rates does not always provide the clearest perspective of this issue or other issues related to employment or changes in total labor costs. Joseph Stalin once said, “A single death is a tragedy; a million deaths is a statistic.” We might paraphrase this logic as it applies to the plight of small businesses, “The death of a single small business is a tragedy; the death of hundreds of thousands is a statistic.”
The impact of changes in minimum wage on employment is a statistic that affects many people. When observing or discussing these values in research studies (e.g., 6.2 percent unemployment rate), one can easily ignore the impact that an increase in labor costs has on a single small business, its owner, and its employees. Thus, it may be worthwhile for future research to focus attention on firm-specific financial performance issues as they relate to the minimum wage and the prospect of a health insurance tax on businesses with payrolls over $250,000 that do not insure their employees. Our research is an introductory effort to shed light on this critical topic. The options we suggested small business owners may choose in response to minimum wage and a health insurance lend themselves to simple hypothesis testing on a future sample of small firms should both issues materialize. They are clearly plausible alternatives to the small business owner that is concerned about rising labor costs, although researchers may want to identify other alternatives as well. It can be stated with relative certainty that most small business owners are not simply going to sit back idly while their labor costs go up without any real improvement in quality or productivity. The real question that remains is exactly what they will do. That is an empirical question that should be considered in future research.

Conclusion

This research provides a discursive assessment of the impact of the federal legislation with regard to minimum wage and the proposed health insurance surcharge on small businesses with $250,000 in labor costs that do not carry health insurance for their employees. We address this original health insurance tax provision because Congress has recently suggested new
provisions may reduce the fifty-employee threshold. We use a typical company in the restaurant industry to evaluate the impact on labor costs. This industry is particularly relevant because it contains a large number of small businesses. These companies have many employees earning minimum wage and working part-time.

We conclude that a firm with as few as 20 employees would have as much as a 50-55 percent decrease in net income as a result of the two federal labor laws discussed in this research. The costs identified in this study are not insignificant because they may become a reality for firms with fewer than 50 employees if the Health Care Bill is modified. The change in the minimum wage law alone can raise labor expenses between $4,709 and $37,677 for firms with between 5 and 40 employees, respectively, according to our findings.

References


## Table 1
Impact of New Minimum Wage Rate on Payroll Costs

<table>
<thead>
<tr>
<th></th>
<th>5 employees</th>
<th>10 employees</th>
<th>20 employees</th>
<th>40 employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>25 hours per week x 50</td>
<td>1250</td>
<td>1250</td>
<td>1250</td>
<td>1250</td>
</tr>
<tr>
<td>Number of Employees</td>
<td>5</td>
<td>10</td>
<td>20</td>
<td>40</td>
</tr>
<tr>
<td>FICA, Medicare</td>
<td>.0765</td>
<td>.0765</td>
<td>.0765</td>
<td>.0765</td>
</tr>
<tr>
<td>Increase in Minimum Wage</td>
<td>$0.70</td>
<td>$0.70</td>
<td>$0.70</td>
<td>$0.70</td>
</tr>
<tr>
<td>Total Payroll Increase</td>
<td>$4,709.69</td>
<td>$9,419.38</td>
<td>$18,838.75</td>
<td>$37,677.50</td>
</tr>
</tbody>
</table>

## Table 2
Impact of Original Medical Insurance Tax on Payroll Costs*

<table>
<thead>
<tr>
<th></th>
<th>5 employees</th>
<th>10 employees</th>
<th>20 employees</th>
<th>40 employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>25 hours per week x 50</td>
<td>1250</td>
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</tr>
<tr>
<td>Number of Employees</td>
<td>5</td>
<td>10</td>
<td>20</td>
<td>40</td>
</tr>
<tr>
<td>FICA, Medicare</td>
<td>.0765</td>
<td>.0765</td>
<td>.0765</td>
<td>.0765</td>
</tr>
<tr>
<td>Minimum Wage</td>
<td>$7.25</td>
<td>$7.25</td>
<td>$7.25</td>
<td>$7.25</td>
</tr>
<tr>
<td>Total Payroll</td>
<td>$48,778.91</td>
<td>$97,557.81</td>
<td>$195,115.63</td>
<td>$309,231.25</td>
</tr>
<tr>
<td>8% Medical Insurance</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>0.08</td>
</tr>
<tr>
<td>Total Medical Insurance</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>$31,218.50</td>
</tr>
<tr>
<td>Impact</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Change in Labor Costs</td>
<td>$8,612.00</td>
<td>$17,224.00</td>
<td>$34,448.00</td>
<td>$68,896.00</td>
</tr>
</tbody>
</table>

* The medical insurance penalty (tax) will only affect companies with payrolls that exceed $250,000 in the current proposals before both houses of Congress. Reaching the threshold of $250,000 depends on the total number of employees, the mix of full- and part-time and their respective hourly wages or salaries. If a firm with 20 employees has 10 full-time workers and 10 part-time employees (25 hours per week), then they will have employee payroll of over $250,000. However, we use a conservative estimate of hours per week and number part-time workers.
Table 3
Impact on Total Payroll Costs

<table>
<thead>
<tr>
<th></th>
<th>5 employees</th>
<th>10 employees</th>
<th>20 employees</th>
<th>40 employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Payroll Increase</td>
<td>$4,709.69</td>
<td>$9,419.38</td>
<td>$18,838.75</td>
<td>$37,677.50</td>
</tr>
<tr>
<td>Total Medical Insurance</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>$31,218.50</td>
</tr>
<tr>
<td>Total Change in Labor Costs</td>
<td>$4,709.69</td>
<td>$9,419.38</td>
<td>$18,838.75</td>
<td>$68,896.00</td>
</tr>
</tbody>
</table>

Table 4
Total Labor Costs with both Full and Part-time Employees

<table>
<thead>
<tr>
<th></th>
<th>Part-Time</th>
<th>Full-Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Part-Time Labor 25 hrs / week @$7.25/hr</td>
<td>8</td>
<td>26</td>
</tr>
<tr>
<td>Full-Time Labor @ 40 hrs/week @ $10.00/hr</td>
<td>8</td>
<td>0</td>
</tr>
<tr>
<td>Total Number of Employees</td>
<td>16</td>
<td>26</td>
</tr>
<tr>
<td>Total Payroll including FICA **</td>
<td>$250,286.25</td>
<td>$253,650.31</td>
</tr>
</tbody>
</table>

** A firm with as few as ten full-time employees earning $12.50 per hour would have a total payroll of $ 269,125, including FICA and Medicare.
BUFFALO WILD WINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS
Fiscal year ended December 28, 2008

<table>
<thead>
<tr>
<th>Revenue:</th>
<th>Consolidated December 28, 2008</th>
<th>One store before change</th>
<th>One store after change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>in thousands</td>
<td>adjusted for 1000s</td>
<td>Percent of Sales</td>
</tr>
<tr>
<td>Restaurant sales</td>
<td>379,686</td>
<td>$1,927,340</td>
<td>89.9%</td>
</tr>
<tr>
<td>Franchise royalties and fees</td>
<td>42,731</td>
<td>$216,909</td>
<td>10.1%</td>
</tr>
<tr>
<td>Total revenue</td>
<td>422,417</td>
<td>$2,144,249</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

Costs and expenses:

| Restaurant operating costs: | | | | |
|------------------------------|-------------------|-------------------|-------------------|
| Cost of sales                | 113,266           | $574,954          | 26.8%             | $574,954          | 26.8%          |
| Labor                        | 114,609           | $581,772          | 27.1%             | $676,504          | 31.5%          |
| Operating                    | 60,205            | $305,609          | 14.3%             | $305,609          | 14.3%          |
| Occupancy                    | 25,157            | $127,701          | 6.0%              | $127,701          | 6.0%           |
| Depreciation and amortization| 23,622            | $119,909          | 5.6%              | $119,909          | 5.6%           |
| General and administrative (1) | 40,151           | $203,812          | 9.5%              | $203,812          | 9.5%           |
| Preopening                   | 7,930             | $40,254           | 1.9%              | $40,254           | 1.9%           |
| Loss on asset disposals and impairment | 2,083            | $10,574           | 0.5%              | $10,574           | 0.5%           |
| Total costs and expenses     | 387,023           | $1,964,584        | 91.6%             | $2,059,316        | 96.0%          |

Income from operations        | 35,394            | $179,665          | 8.4%              | $84,933           | 4.0%           |
Investment income             | 970               | $4,924            | 0.2%              | $4,924            | 0.2%           |

Earnings before income taxes  | 36,364            | $174,741          | 8.1%              | $80,009           | 3.7%           |
Income tax expense            | 11,929            | $60,553           | 2.8%              | $28,344           | 1.3%           |

Net earnings                  | 24,435            | $114,188          | 5.3%              | $51,665           | 2.4%           |

Source: Buffalo Wild Wings, Inc. Form 10-K