Use wage hike, EITC to help Delawareans

The issue of whether to increase the minimum wage is in the news. In November, fast-food workers in Delaware staged a one-day protest in support of a higher minimum. President Obama has proposed an increase to $10.10 by 2015, up from $7.25. And in the Delaware legislature, there is a move to raise the state minimum wage this session.

DELAWARE VOICE

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Low-wage workers have been largely left out of the economic progress of the past few decades, while income inequality has increased substantially. After adjusting for inflation, the current minimum wage is more than a dollar lower than it was in 1979. It has already dropped 58 cents in purchasing power since it was last increased in 2009.

For many years, the received wisdom about minimum wages from Econ101 was "proceed at your own risk." A higher minimum wage was a two-edged sword. It might increase earnings for some, but at the cost of reducing employment opportunities for others. The consensus estimate from research that examined changes over several decades was that a 10 percent increase in the minimum wage reduced teen employment by about 1 percent to 3 percent. That's not huge, but it is negative.

This research was questionable, however, because it could not convincingly sort out what part of the employment change was due to minimum wage increases and what was due to other social and economic factors. Newer research has focused, instead, on comparing employment changes in places where the minimum wage was raised to the corresponding changes in places with no increase. An early famous example examined fast-food restaurant employment in New Jersey and Pennsylvania after New Jersey increased its minimum wage in 1992. That analysis actually found that employment increased after the minimum wage increased.

Another well-known recent study compared employment in adjacent counties across state lines, where the states had different minimum wages. It, too, found no negative effect on employment.

It is now clear that modest increases in the minimum wage do not have negative effects on employment. This research does not mean, however, we can raise the minimum wage higher and higher without adverse consequences. Based on the research to date, an increase of 20 percent to 25 percent phased in during two years is probably the upper limit.

At this point, the biggest problem with a minimum wage increase is that over time it has become a less efficient means of channeling income to low-income families.

For that reason, the Earned Income Tax Credit is in some ways a preferable way to assist low-income working families. The EITC is a very successful Federal program that provides income support through the tax system to families with low-to-moderate earnings. Because a family typically files a single tax return that combines the earnings of all members, the EITC is better targeted at low and moderate income families. In 2013, the EITC was worth more than $5,000 for a family with two children and earnings between $13,430 and $17,530.

Like 25 other states, Delaware has a state EITC that piggy-backs on the Federal program. But the design of Delaware's program was deeply flawed from its inception. It excludes from benefits the neediest families who would otherwise be eligible, because they typically earn too little to owe Delaware taxes. (Technically, the problem arises because the Delaware EITC is non-refundable, unlike the Federal program and 21 states.) Even worse, the Delaware EITC limits the benefits that eligible families receive, because it bases the credit on the earnings of only one spouse, even if both work and are EITC-eligible.

If I were designing a legislative program to assist low- and moderate-income working families in Delaware, I would focus on two things. First, because it is unlikely that Republicans in Washington will agree to the minimum wage increase proposed by President Obama, Delaware can and should act on its own. A 25 percent increase, phased in over two years, would bring the minimum wage to just mor than $9. The minimum should also be indexed, so it automatically increases with inflation. Second, Delaware should review its EITC program. The technical correction to include the earnings of both spouses can be done at modest cost. Making the EITC fully refundable would be far more costly, but steps can be taken in that direction.

This is a rare situation in which politics and economics have largely aligned. Delaware ought to act now to assist its low- and moderate-income working families.

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