

Proposition I-02-2024
One Fair Wage Act
Fiscal Analysis

Estimated Impact

A.R.S. § 19-123(E) requires the JLBC Staff to prepare a summary of 300 words or less on the fiscal impact of voter-initiated ballot measures. Arizona's minimum wage is currently adjusted each year for the increase in the cost of living. Proposition I-02-2024 would further raise the state's current hourly minimum wage by an additional \$1.00 in 2025 and by another \$1.00 in 2026. The proposition would also phase out the current allowance in the minimum wage for tipped employees.

The initiative's provisions may have an economic impact on state and local revenue collections and state and local spending. By increasing wages and business costs, the proposition may affect individual income tax, corporate income tax and sales tax collections. In addition, the initiative's provisions may affect participation in, and the cost of, public assistance programs. The proposition may also affect the cost of state contracts with vendors if the vendors employ minimum wage workers. The impacts of the proposition on either state and local revenues or state and local spending cannot be determined in advance.

Analysis

Arizona law requires employers to pay a minimum wage of \$14.35 an hour in 2024. Current law also allows employers to pay up to \$3.00 less than this hourly minimum wage to tipped employees as long as the combination of wages and tips at least equals the minimum wage.

Impact on Businesses

The proposition's additional increase in the hourly minimum wage and the elimination of the deduction for tipped wages may result in higher labor costs for businesses in Arizona. To compensate for the higher wage costs, businesses may attempt to raise product prices, reduce other labor costs (e.g., non-wage benefits), and/or substitute capital for labor through automation. If they are unable to pass on the higher labor costs to consumers or raise their productivity, businesses may experience reduced profits and possibly reduced operations in the state. This could result in a decline in both employment and business activity.

Impact on Wage Earners

The initiative would directly benefit employees through the additional \$1.00 increases in 2025 and 2026 and the elimination of the allowance for tipped wages. This impact could be offset if employers respond to these adjustments by reducing their payroll costs, either through a reduction in employee hours or a reduction in the number of employees.

There is considerable academic research on the effect of minimum wage increases on employment. As noted by the federal Congressional Research Service in their 2021 review of the academic literature, "broadly speaking, there is not universal consensus on the causal relationship between changes in minimum wage and other economic outcomes". In addition to a lack of overall consensus in the academic research, available studies also do not replicate the ballot initiative's specific minimum wage proposal. As a result of all these factors, the impact that the proposition's minimum wage increases would have on employment is highly uncertain.

Impact on Consumers

Consumers may also be affected by the proposed minimum wage increase if businesses increase their product prices in response to the associated labor cost increase. In other words, some businesses may pass along the cost of the wage increase to their customers. However, other businesses may absorb the higher labor cost stemming from the minimum wage increase without raising prices.

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Impact on State Revenues

The academic minimum wage studies do not generally attempt to quantify the overall tax revenue impact of a minimum wage increase. As noted below, a higher minimum wage could theoretically have different effects on state individual income and corporate income taxes and sales taxes. As a result, the overall impact on state revenue collections cannot be determined in advance.

Individual Income Tax

Those employees receiving a higher wage would pay a higher amount of state individual income tax than under current law. However, some of these revenue gains may be offset if there is any negative employment effect associated with the minimum wage increase, such as a reduction in employee hours or the number of employees.

Corporate Income Tax

The higher labor costs associated with a minimum wage increase may result in reduced corporate profits, which, in turn, may reduce state corporate income tax payments. The tax revenue impact depends on the extent to which corporations would be able to offset the cost increase by raising product prices, reducing other labor costs (e.g., non-wage benefits), and/or substituting capital for labor through automation.

Sales Tax

Those individuals who benefit from the proposed minimum wage increase would have a higher disposable income, which, in turn, may result in increased spending and thus higher sales tax revenues for the state. The opposite scenario would occur for those individuals who experience a reduction in hours or job loss as a result of this proposal. Sales tax revenues could also increase as a result of businesses raising their product prices in response to the minimum wage increase.

Impact on State Expenditures

A higher minimum wage could potentially affect participation in Arizona Health Care Cost Containment System (AHCCCS) and Department of Economic Security (DES) programs in which eligibility is determined by income level. This impact could be the result of 2 differing factors: 1) The wage increase could generate state savings if employees receiving higher wages reduces the number of individuals who rely on public assistance; and 2) The wage increase could generate state costs if there are negative employment effects that increase the number of citizens who rely on the public assistance. This net impact cannot be determined.

Under the proposition, the state government as an employer would remain exempt from paying the minimum wage. The state may be impacted, though, through its contracts with companies employing non-state workers. If contractors' wages are below the new proposed minimum wage and are increased by the initiative, state contracted costs may increase as contractors raise wages.

Local Government Impact

The Urban Revenue Sharing formula distributes 18% of income taxes collected 2 years prior to incorporated cities and towns. Depending on how the wage increase impacts income tax revenues, these distributions could change starting in FY 2027. State sales tax revenues are also shared with local governments. Any change in these collections resulting from the proposition would impact distributions to cities and counties starting in FY 2025.

Unlike the state government, political subdivisions are currently required to pay the Arizona state minimum wage rate. Therefore, political subdivisions may incur additional employee payroll costs. In addition, if the proposition increases the labor costs of contractors, political subdivisions may also incur additional contracting costs.

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