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**SFA****BILL ANALYSIS**

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Senate Bill 208 (as reported without amendment)  
Sponsor: Senator Dale L. Shugars  
Committee: Finance

Date Completed: 3-3-97

### **RATIONALE**

The minimum wage in Michigan has not been changed since 1981, although the Federal minimum wage recently was increased. This spurred efforts in Michigan to raise the State's minimum wage rate, in a like manner, for those persons not covered by the Federal increase. (The Federal minimum wage applies in Michigan to all employees of businesses with annual revenue over \$500,000 that produce goods for sale outside the State. The Federal law also covers other types of employers, including State and local government.) As a result, Senate Bill 1 and House Bill 4177 were passed by the Legislature to raise the State's minimum wage.

During debate over development and passage of the bills much of the discussion involved the treatment of restaurant servers. Servers have traditionally had a minimum wage rate that is lower than the minimum wage for other employees in recognition of the fact that servers receive tips. In Michigan, tipped employees covered by the State's Minimum Wage Law must be paid \$2.52 per hour, while other workers must be paid \$3.35 per hour. (If a tipped employee does not receive tip income, that is sufficient when combined with the hourly wage to meet the minimum wage rate for other workers, then the employer must increase the employee's hourly wage until the combination of tips and wage equals that minimum wage rate.) The State's \$2.52 hourly rate for tipped employees is higher than the \$2.13 per hour Federal requirement set for tipped employees. Under Enrolled Senate Bill 1 (which has not yet been signed by the Governor), the minimum wage for non-tipped employees would be increased to \$4.75 on May 1, 1997, and \$5.15 on September 1, 1997. The minimum hourly wage would be \$2.65 for an employee who received gratuities, if the gratuities exceeded the difference between \$2.65 per hour and the minimum hourly wage established for other employees.

Food servers in Michigan receive an average of \$5.48 per hour in tips, according to the Michigan Restaurant Association, for an average hourly rate of around \$8 per hour when combined with the minimum wage. It has been pointed out that, for persons trying to get off welfare or for those entering the job market for the first time, food service jobs are often available and offer decent pay. While some people contend that raising the minimum wage for typical employees by 13 cents an hour (from \$2.52 to \$2.65 as proposed in Senate Bill 1) is only fair, others believe that many restaurant owners, particularly small operations, would find the increase burdensome and would have to reduce their workforce. It has been suggested that an alternative way to increase the pay of servers, while not increasing the payroll of employers, would be to allow a deduction from income tax liability of a certain amount of gratuities received by servers.

### **CONTENT**

The bill would amend the Income Tax Act to allow a taxpayer to deduct, to the extent included in the taxpayer's Federal adjusted gross income, up to \$10,000 in gratuities in a tax year if the minimum hourly wage that could be paid to the taxpayer, under the Minimum Wage Law, were \$2.52 per hour. "Gratuities" would mean tips or voluntary monetary contributions received by an employee from a guest, patron, or customer for services rendered, and that the employee reported to the employer for purposes of the Federal Insurance Contributions Act (FICA). The deduction would apply to the 1997 tax year and thereafter.

MCL 206.30

### **ARGUMENTS**

*(Please note: The arguments contained in this analysis originate*

### **Supporting Argument**

Recent changes to the Federal minimum wage have prompted efforts in Michigan to increase the minimum wage for those Michigan workers who are not covered by the Federal law. Since the State minimum wage has not been changed since 1981, it would seem that the 13-cent hourly increase proposed in Senate Bill 1 for tipped employees would be a well deserved increase. The proposed increase, however, must be looked at from the employer's standpoint as well as the employee's. Many food service establishments in this highly competitive industry operate on a slim profit margin; thus, raising the minimum wage by 13 cents per hour per server could have a devastating effect on many restaurants. In light of what could be gained by increasing the wages of servers a mere 13 cents per hour, that increase would seem unwise when one considers what could be lost in terms of fewer positions and perhaps fewer establishments. By allowing tipped employees to deduct up to \$10,000 in gratuities received, Senate Bill 208 would provide servers with an increase in take-home pay but do so without increasing employers' payrolls. Thus, the bill would create a benefit for this deserving segment of the working population, while not increasing the burden on employers.

**Response:** If Senate Bill 1 is signed by the Governor, Senate Bill 208 will have no effect, since it would apply only if the minimum wage that may be paid to tipped employees were \$2.52.

### **Supporting Argument**

Providing a substantial deduction for tipped employees would create an additional incentive for unemployed persons, first-time job seekers, and welfare recipients to take jobs in the restaurant and hospitality industry. These positions have several advantages for single parents, students, and other persons with few resources. Many food service positions offer flexible hours, often allowing parents to work during school hours and thus save money on child care expenses; such positions can often produce an income that is higher or substantially higher than the minimum wage; and persons taking entry level positions as servers can often move rapidly into managerial or other positions in the industry. The bill, through its promise of allowing servers to take home a greater proportion of their pay, would enhance all of these advantages, as well as provide an incentive for persons already in the industry to stay in the industry and work even harder.

### **Opposing Argument**

While any effort to help low paid workers is to be applauded, it must be asked whether the bill's proposed deduction and the resulting foregone tax revenue would be the best way to help. By limiting the deduction to employees who receive gratuities, the bill would primarily benefit one group, food servers, while ignoring all other low-paid workers. This means that some low-paid workers would receive a tax benefit that other low-paid workers could not claim, based simply on how they earned the income. In addition, what of cooks, dishwashers, and other persons who are making minimum wage and working side by side with servers? It is not clear why tipped employees, who are likely making more than the dishwashers, etc., should be given a tax break when those working beside them are not. There are other ways to help low-paid workers without discriminating against some workers, such as through increasing the earned income credit or the personal exemption, or increasing the minimum wage as proposed in Senate Bill 1.

### **Opposing Argument**

The bill would have substantial revenue implications, but it is questionable how much it would benefit those persons to whom it is targeted. For instance, it has been said that a single mother earning \$10,000 in tips would realize a gain of \$440 per year in lower taxes. Yet it must be pointed out that a single mother with two children, and thus three exemptions, would pay no State income tax on wages and/or tips anyway on income up to \$7,200. Many people believe that the woman, or persons in similar situations, would be better off with the proposed increase in the minimum wage, or other form of tax relief.

Legislative Analyst: G. Towne

### **FISCAL IMPACT**

The State fiscal impact would be a reduction of income tax revenue of \$11.6 million, which would result in a \$2.7 million loss in the School Aid Fund (SAF), and an \$8.9 million loss in the General Fund.

Fiscal Analyst: R. Ross

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