

teaching note

Surviving the Minimum Wage Increase: A Case Study Of An Independent Restaurant

Summary

Julio is the owner and manager of a popular, independent Mexican restaurant in San Francisco Bay Area, California. As the City of San Francisco has increased the minimum wage to reflect the heightened living cost, Julio has to follow the city policy. In order to address this situation and continue to thrive in the industry, Julio needs to make some changes in his restaurant operation. He has five options: 1) increasing the menu prices, 2) reducing the food portion/cost, 3) implementing break time between lunch and dinner, 4) eliminating the hosts, and 5) fully automating the front-of-the-house and eliminating hosts and servers. Julio needs to weigh the pros and cons of these options and decide what is best for his restaurant to minimize the risks and maximize the profits.

Theoretical Background

The federal minimum wage provisions are part of the Fair Labor Standards Act (FLSA), which was enacted by the federal government. From 1938 to 2009, the federal government had continuously increased the federal minimum hourly wage starting at \$0.25 per hour in 1938 to reach \$7.25 per hour in 2009 (United States Department of Labor, 2018a).

Over the past couple of years, there has been an upsurge in the number of municipalities that have passed minimum wage ordinances allowing for higher rates than the state minimum wages. As a result, the number of mandatory city and county labor law posters has increased significantly (Poster Compliance Center, 2018). Specifically, about 40 counties and cities have set their own minimum wage laws (LaborLawCenter, 2018; UC Berkeley Labor Center, 2018).

Minimum wage increases significantly affect the restaurant industry. A 10% increase in the minimum wage is likely to reduce skilled employment by 2-4% and the total restaurant employment by 1-3% (DePillis, 2018; Dorn, 2013). Moreover, it is predicted that a \$1 increase per hour in the minimum wage leads to a 4-10% increase in the exit rate for restaurants rated by an online review website with an average of 3.5-star rating but has no significant impact for those restaurants with a 5-star rating (Luca & Luca, 2017). Also, higher minimum wages would negatively affect the rate at which new restaurants open by 4-6% (Luca & Luca, 2017). Considering that labor costs account for 30-40% of the total cost of operation in table service restaurants (Buckley, 2018), the proposed increase in minimum wage could adversely affect these restaurants.

Target Audience

The target audiences of this case study are undergraduate and graduate students studying hospitality management and related fields.

Specifically, relevant undergraduate courses are Introduction to Hospitality Management, Hospitality Law, Human Resource Management, and Food Service Management. Graduate courses may include Advanced Human Resource Management and Advanced Food Service Management. In addition, it is recommended that the instructor assigns a critique paper on one of the additional readings in the Case Study section.

Teaching Objectives

With the completion of the case study and the related activities, students will be able to:

- Analyze the effects of the minimum wage increase on restaurant businesses and employees
- Evaluate the pros and cons of potential solutions for the minimum wage increase from a managerial perspective
- Develop strategies to overcome financial issues regarding the minimum wage increase in restaurant businesses
- Conduct supplementary research on the impact of increased minimum wages on independent businesses and employees (graduate students only)

Instruction Plan

The case study can be fully understood when taught throughout one class session lasting about an hour and a half. In addition, it is recommended that the instructor informs students about reading and understanding the case study and being prepared to answer the discussion questions prior to class.

Part 1 - Introduction and Review of Concepts - 20 minutes

Start the class by asking students to share whether they have any experience in working at a restaurant. Introduce the basic concepts that are related to the topic of this case study as follows:

- Minimum wage: Minimum wage is defined as the minimum sum payable to a worker for work performed or services rendered, within a given period, whether calculated on the basis of time or output, which may not be reduced either by individual or collective agreement, which is guaranteed by law and which may be fixed in such a way as to cover the minimum needs of the worker and his or her family, in the light of national economic and social conditions (International Labor Organization, 1992).
- Exempt employees vs. nonexempt employees: The term "exempt employees" refers to the employees that are not affected by the minimum wage or overtime policies by the Fair Labor Standards Act (FLSA) (Hayes & Ninemeier, 2009). These employees are not paid hourly but paid with salary. An example of exempt employees is chefs that work on annual salary in

restaurants. On the other hand, nonexempt employees are affected by the minimum wage or overtime policies by the Fair Labor Standards Act (FLSA) and paid hourly (Hayes & Ninemeier, 2009). Examples of nonexempt employees include restaurant servers and hosts.

- Tipped employees vs. non-tipped employees: Tipped employees refer to those who regularly and customarily receive more than \$30 per month in tips (United States Department of Labor, 2018e). Non-tipped employees are those who rely on their hourly wages as their main source of income, and generally do not receive any tips or gratuities (Johnson, 2005).
- Automation in the foodservice industry: “At table” ordering and self-ordering provide convenience and order accuracy for customers which allow restaurants to be more efficient and to save labor costs. Restaurants can use a POS system at tables to create a one-stop experience for customers by allowing them to order, pay and even sign up for a loyalty program in their seats. By speeding up the ordering process, restaurants can potentially increase sales by eliminating the waiting time involved to order (Restaurant Engine, 2015). Moreover, a POS system simplifies the communications between the kitchen and the wait staff as orders go through computers, directly to the kitchen (Mealey, 2018).
- Employee job satisfaction: Job satisfaction is the feeling one has when he or she enjoys their job (McMillan Dictionary, 2018) and represents a combination of positive or negative feelings that workers have towards their work (Davis & Newstrom, 1985).

Next, briefly introduce the current minimum wage policy change in the U.S. and discuss its impact on restaurant employers and employees. Let the students discuss whether there are any factors affecting customer satisfaction with regards to the minimum wage increase.

Part 2 - In-class Activity (Discussion) - 50 minutes

The instructor can divide students into groups depending on the number of students in class and assign one of the solutions described in the Case Study section for each group. When assigning solutions, all solutions need to be equally distributed for each group. First, students can evaluate the pros and cons of their assigned solution and compare them with the pros and cons of all the other solutions in order to justify how and why their solution would be the best option to choose for the restaurant in the case study. Students should be able to come up with compelling arguments to support their assigned solution. Then, have the students nominate one representative from each group to discuss their rationale for their choice and defend their arguments through a debate. However, if there is more than one group for a solution, invite an equal number of representatives per solution. The purpose of this exercise is to help students analyze the pros and cons of each possible solution and understand the impact of minimum wage policy on restaurants. Students can also practice their debating

skills by working on making sound arguments and rebuttals for their stance. In addition, encourage the students to discuss the potential impacts of the minimum wage increase on restaurant workers’ performance and job satisfaction.

Part 3 - Summary - 20 minutes

Restate the main objective of this case study and provide a brief summary of the basic concepts and the possible solutions. Revisit the pros and cons of each solution that were discussed during the debate. Also, ask the students their opinions on which solution would be the ultimate choice for this case study by conducting a vote. Last, wrap up the class by assigning a two-page essay to discuss the best solution each student would choose and have them justify their arguments with appropriate references. Also, the instructor may allow them to earn extra credit if they are able to present any other solutions in addition to those discussed in class. Another essay on summarizing a relevant academic article or industry news article and presenting their opinions on the minimum wage increase may be given to graduate students as an additional assignment.

Assessment

By participating in discussions, students will be able to demonstrate their abilities to analyze the effects of the minimum wage increase on restaurant businesses and employees (teaching objective 1). The assigned two-page essay will allow the instructor to evaluate whether the students can compare the pros and cons of possible solutions (teaching objective 2) and propose the best option for the restaurant (teaching objective 3). For graduate students, the instructor can evaluate their critical thinking skills by giving them an additional assignment to conduct supplementary research on the impact of the minimum wage increase on independent businesses and employees (teaching objective 4).

Analysis of Discussion Topics and Questions

Below is the analysis of the discussion questions included in the case study:

1. *Will the increase in minimum wage affect independent restaurants positively or negatively? Why or why not?*

Answers may vary among students. Some students may assert that the increase in minimum wage will affect independent restaurants negatively as they are smaller and more vulnerable to change compared to chain restaurants. The increased minimum wage may impose a financial burden for independent restaurants as they struggle to match the incomes of their employees to the increased minimum wage. Others may argue that there can be positive impacts on the restaurants in the long run as higher minimum wages will contribute to the higher buying power of consumers, thus, compensating for the initial loss of profits due to increased labor costs.

2. *Will the minimum wage increase affect the job satisfaction of the restaurant employees? Discuss the possible pros and cons from the perspective of employees.*

The answers may vary depending on where the employees' priorities lie. If the employees are focused on the work environment or their fellow employees, then the minimum wage increase will not have a significant impact on their job satisfaction. However, when employees are more concerned about receiving compensation, rewards, or wages, then the minimum wage increase can affect employee job satisfaction. With the increased income, employees would be able to spend more which can lead to a circulation of money in the economy affecting other businesses along the way. In addition, if an employee is an exempt employee getting paid with a salary, his/her job satisfaction may not be affected by the minimum wage increase. However, if the employee is a nonexempt employee whose income is tied to the minimum wage paid by the hour, his/her income would be affected and therefore their job satisfaction will be affected as well.

3. *Identify the benefits and challenges of each of the 5 solutions offered.*

Five possible solutions were suggested in the case study including 1) increasing the menu prices, 2) reducing the food portion/cost, 3) implementing break time between lunch and dinner, 4) eliminating the hosts, and 5) fully automating the front-of-the-house and eliminating hosts and servers.

Each solution has benefits and challenges, and these answers should vary depending on the students.

For increasing the menu prices, some students may argue that this solution will help Julio earn extra profits to compensate for the increased labor costs. However, others may refute by saying that restaurants might experience difficulty in attracting new customers and risk the loss of existing customers as some of them may complain or even stop coming to the restaurant due to the increased prices. Moreover, this may result in lower tips for wait staff if customers notice the price increases, are aware that the minimum wage has been increased for the employees, and believe that tipping is no longer necessary, as a result.

For the second option where Julio chooses to reduce the portions of some menu items, some students may support the idea by asserting that Julio would be able to cut down on the food costs by reducing the portions of some high-cost menu items such as beef steak or seafood dishes. These items are relatively expensive and smaller portions may compensate for the losses resulting from the increased labor costs. However, there could be others opposing the solution as it may result in complaints and dissatisfaction from existing customers who notice that portions have been reduced compared to previous visits.

The third option involves implementing a break time between lunch and dinner operations. While some students may favor the solution as it allows the restaurant to have more time to prepare for the dinner operation and save some labor costs by reducing the hours of operation, others may argue that this can potentially affect the number of customers and sales to decrease, consequently.

Some students may choose the fourth solution asserting that getting rid of hosts entirely would allow Julio to save on labor costs. However, others may argue against it saying that this could cause some existing customers to feel that the service quality has gone down compared to the past. In this case, the existing customer satisfaction and visit frequency could be negatively affected. Moreover, this option could affect the employees' productivity as it can generate an unnecessary fear of losing their own jobs.

Last, some students may support the fifth option which suggests full automation of the front-of-the-house using a POS system. By fully automating the front-of-the-house and eliminating all hosts and servers, Julio may be able to save a tremendous amount on labor costs and boost the productivity of the restaurant. However, other students may oppose the solution because Julio will need to bear the cost of the installation and maintenance fees, which may not be a good investment. In addition, the number of customers may decrease because some customers who are not tech-savvy may feel awkward and less comfortable relying entirely on the POS system. Such a system would ultimately change the ambiance of the restaurant.

4. *Considering the benefits and challenges of each option, what would be the best choice for Julio's restaurant that would minimize the risk and maximize the profits? Justify your answer.*

Students' answers will vary depending on the pros and cons they have identified for each solution. Some students may support the first solution as Julio can offset the increased labor costs with extra income resulting from increasing the menu prices without getting rid of any employees. Also, the second solution, which reduces the portion size of certain menu items, could be chosen as the best option because it allows Julio to save on the food costs and use the extra profits to compensate for the increased labor costs without compromising the food quality or harming the employees. Implementing a break between lunch and dinner operations may be favored as the best option by some students. Not only would this option help save the labor costs by reducing the number of operation hours, but it would also give the restaurant a chance to improve their food and service quality because they are able to prepare better for the dinner operation which generally receives more customers than the lunch operation. Some students may feel that the

fourth solution of getting rid of hosts entirely from the restaurant is the best option. Customers would seat themselves and servers would be dealing only with taking the order, bussing, and transactions. This would allow the restaurant to reduce the labor costs without hurting the food quality. Finally, the fifth solution may be chosen where Julio eliminates all front-of-the-house employees and implements full automation of the front-of-the-house. This would save the labor costs and help boost the productivity of the restaurant.

Analysis of the Teaching Objectives

1. *Analyze the effects of the minimum wage increase on restaurant businesses and employees*

Students will be able to understand how the minimum wage increase affects restaurant businesses and employees by assessing the pros and cons.

2. *Evaluate the pros and cons of potential solutions for the minimum wage increase from a managerial perspective*

Through the case study, students will be able to assess each solution and analyze their benefits and challenges to the restaurant. Then, the students will be able to understand how they can effectively apply these solutions to maximize the profits and minimize the costs from a managerial perspective.

3. *3. Develop strategies to overcome financial issues regarding the minimum wage increase in restaurant businesses*

By thinking about the solutions provided, students will be able to analyze the financial status of the restaurant and come up with the best solution that will help solve the issue.

4. *4. Conduct supplementary research on the impact of increased minimum wages on independent businesses and employees*

By conducting supplementary research on the minimum wage increase, graduate students will be able to gain a deeper understanding of the impacts the change may bring to the industry; furthermore, the students will be able to develop research ideas related to an up-to-date topic.

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