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Inside Monopsony: Employer Responses to Higher Labor Standards in the Full Service Restaurant Industry

T. William Lester, Assistant Professor

Center for Urban and Regional Studies
The University of North Carolina at Chapel Hill
Campus Box 3410, Hickerson House
Chapel Hill, NC 27599-3410
Telephone: 919-962-3074 FAX 919-962-2518
curs.unc.edu

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T. William Lester
Assistant Professor
Department of City and Regional Planning
University of North Carolina, Chapel Hill
320 New East (MC #3140)
Chapel Hill, NC 27516
twlester@unc.edu
919-962-3512

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ABSTRACT

While efforts to increase the minimum wage have stalled at the Federal level, dozens of cities have passed or are considering local increases that will bring the minimum wage up to $15 per hour. The pace and scale of recent wage increases—spurred on by an organizing drive by fast food workers in the "Fight for $15" movement—leave policy makers and analysts wondering about their eventual impacts. While the impact of publicly mandated labor standards on employment is well studied and remains highly controversial, there are still important missing pieces in our understanding of how locally-enacted labor laws impact the labor market. Although previous research shows that moderate increases in the minimum wage do not result in net job losses and reduces labor turnover in the aggregate, there is still uncertainty as to how higher labor standards may reshape employment practices within firms. Recent studies show support for a model of the labor market that is monopsonistic rather than perfectly competitive using county-level data aggregated for low-wage industries (e.g. restaurants) or groups of workers (e.g. teens). This paper directly examines employer responses to higher labor standards through a qualitative case comparison of the full service restaurant industry across two fundamentally different institutional settings. Research was conducted in San Francisco—where employers face the nation's highest minimum wage, no tip credits, a pay-or-play health care mandate, and paid sick leave requirements—and in North Carolina's Research Triangle region—where there are no locally enacted labor standards. Consistent with the monopsonistic model, evidence shows that higher labor standards led to wage compression in San Francisco even while some employers continued to offer greater benefits to reduce turnover. Employers in San Francisco exhibit greater investment in finding better matches and tend to seek higher-skilled, more professional workers, rather than invest in formal in-house training. Finally, higher wage mandates in San Francisco have exacerbated the wage gap between front-of-house and back-of-house occupations—which correlate strongly with existing racial and ethnic divisions. Initial evidence shows that some employers have responded by radically restructuring industry compensation practices by adding service charges and in some cases eliminating tipping.

KEYWORDS: Labor Standards; Restaurants; Minimum Wage Adjustment Mechanisms.

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1. Introduction

As the economy slowly recovers from the depths of the Great Recession, the labor market continues to show weakness even as the unemployment rate has fallen to a three-year low. Despite optimistic accounts of the 're-shoring' of manufacturing and a recovering housing market, inequality is on the rise as the majority of jobs created since the official end of the recession in 2009 are relatively low-wage and are in comparatively place-bound service industries such as restaurants, retail and entertainment (NELP 2013). These 'residentiary' jobs often pay low wages, and there has been near-zero growth in real wages for the lowest-paid workers in the U.S. (Mishel & Shierholtz, 2013). A unique feature of this recovery is the "missing middle" in the pattern of job growth with relatively few new middle-income positions or career pathways for workers who lack advanced skills. As a result, an increasing number of workers remain in low-wage positions for longer periods of time, making jobs widely viewed as "stepping-stone" positions into relatively permanent placements (Hyatt & Spletzer, 2013). Arguably, conditions in the low-wage service sector are at a historically low level with stagnant wages, uncertain working conditions and hours, and a hostile regulatory environment towards organized labor. Given these trends, a central concern for policy makers is what can be done to reduce wage inequality? One of the only direct policy responses to this problem has been to increase the minimum wage. As efforts to increase the minimum wage stall at the Federal level, many large cities including Seattle, Los Angeles, San Francisco, and Chicago have passed or are considering local increases that will bring the minimum wage up to $15 per hour. The pace and scale of recent wage increases—spurred by an organizing drive by fast food workers in the "Fight for $15" movement—leave policy makers and analysts wondering about their eventual impacts (Holzer, 2015).

The restaurant industry, which employs more than 9.9 million workers, epitomizes the trend of relatively high growth and low job quality and is arguably the sector most impacted by recent minimum wage increases[1]. Recently, the issue of job quality in the restaurant industry has garnered national attention, as evidenced by the media coverage of a series of fast-food worker strikes and the high-profile research and advocacy of the Restaurant Opportunity Center (ROC). However, these recent efforts to increase wages and benefits follow two decades of attempts to improve labor standards through passage of a host of minimum wage, living wage, and related legislation at the city and state levels (see Reich, Jacobs, & Dietz, 2014). In addition, there are efforts underway in several states to pass other labor

[1] According to the data from the Quarterly Census of Employment and Wages series of the Bureau of Labor Statistics (BLS) there were 9,904,924 workers in the NAICS 722, which ranked as the largest three digit industry by employment in the 1st quarter of 2013. Average weekly wages was $307.

standards, such as raising the wage paid to tipped workers, or mandating paid sick leave. While the impact of publicly mandated labor standards on employment and other labor outcomes is well studied and continues to be debated among economists and policy makers, there are still important missing pieces in our understanding of how locally enacted labor laws may have deeper impacts not only on aggregate outcomes but also on the way employment relationships are structured within firms.

The empirical minimum wage literature is vast and has been evolving since the 1970s, yet most of the literature on the minimum wage, and other labor standards, focuses on only one aspect of their impact—namely on employment. The majority of this work is highly quantitative and relies on aggregate data sources, including the Quarterly Census of Employment and Wages (QCEW) or the Current Population Survey (CPS), to analyze policy impacts at a state or county level (see Andrajit Dube, Lester, & Reich, 2010; Neumark & Wascher, 2006).[2] As a result, economists must use estimated employment elasticities from industry-wide data or from defined demographic groups to make inferences about firm behavior. However, in many ways the behavior of actual firms remains a "black box" for researchers in the field. In addition, there are many ways, beyond just the level of employment, that raising labor standards could impact the employment relationship. These other employment outcomes may include changes to the rate of turnover, productivity, training, tenure, industry-specific norms and performance expectations.

An additional motivation for this study stems from current policy debates. In the last year, following the passage of a $15 "living wage" at Seattle's SEATAC airport, several cities have initiated plans to raise their minimum wage to $15 per hour—a level significantly higher than current rates and well above the historical levels. The potentially large increases in local wage standards are unprecedented in terms of the magnitude of the increases and their potential to significantly alter labor practices in low-wage industries.[3]

This paper directly addresses the question of how firms react and adjust to higher labor standards such as minimum wage increases and mandated health care spending. To do so, this paper employs a mixed methods comparative case design that analyzes employment practices across the restaurant industries in two institutionally divergent urban labor markets: San Francisco, which has the nation's strongest local labor standards, and North Carolina's Research Triangle, which has no locally mandated regulations. These institutional differences have result in extreme differences in the mandated wage and

[2] While research such as Fairris (2005), Dube, Naidu, and Reich (2007), and Reich, Hall and Jacobs (2005) use firm-level data derived from city contracts or surveys they either examine a relatively narrow set of employment outcomes or do not focus directly on restaurants.

[3] Specifically, Seattle passed a new law that will raise the minimum wage to $15 by 2015 and San Francisco voters will decide on a proposal to an increase the minimum wage to $15 from $10.55 per hour. The percentage increases involved (61 and 42) are above all of the state and local increases included in our previous national studies (Dube, Lester, Reich 2010, 2013).

benefit levels that employers must offer. Ultimately, this paper finds that higher labor standards—including a high minimum wage with no tip-credit, mandated healthcare contributions and paid sick leave—led to wage compression both within firms and across the restaurant industry in San Francisco. Yet, there is also evidence that some employers in San Francisco still offer compensation above the mandated minimum in order to attract workers. In addition, employers in San Francisco exhibit greater investment in finding better matches and seeking higher skilled, more professional workers, rather than investing in formal in-house training. Finally, higher wage mandates have exacerbated the wage gap between front-of-house and back-of-house occupations—a division of labor that correlates strongly with existing racial and ethnic divisions. Initial evidence shows that some employers have responded by radically restructuring industry compensation practices by adding service charges and in some cases eliminating tipping. Collectively, these findings provide empirical support for both monopsonistic and institutional accounts of firm behavior in local labor markets, which should be accounted for in any prospective analysis of labor standards.

2. Theoretical Context and Previous Research

The current theoretical landscape of the labor market remains disjointed. On the one hand, the economics profession is still dominated by the neoclassical viewpoint which treats the market for labor much like the market for other goods in the economy—with firms as relatively passive price takers and workers moving freely between jobs to maximize their utility. In this view, the labor market is constantly in equilibrium and any attempt to raise standards through public policy (e.g., the minimum wage) will result in job losses. Since the mid-1990s, however, economists have begun to propose an alternative model of the labor market based on the theory of monopsony which implies that firms have some degree of market power which leads to latitude in setting wage levels, which allows them to choose from a variety of human resource practices to match their competitive strategy (Boal & Ransom, 1997; Burdett & Mortensen, 1998; Manning, 2003). The dynamic monopsony model posits that, due to "frictions" in the labor market (i.e. the cost of searching for a new job, geographic constraints, the cost of turnover, etc.) we can expect to see variation in firm practices even within the same industry as some employers attempt to hold on to their workforce by paying higher wages and/or benefits (to reduce turnover) and others may choose a "low-road" strategy of low wages and high turnover. This set of models is used to explain the empirical findings that policy interventions such as minimum wage increases and living wage standards do not significantly reduce aggregate employment.

2.1 Monopsony and Low-wage Labor Markets

Interest in empirically detecting the existence of monopsony power was sparked by the work of Card and Kruger (1995) who were the first to show that minimum wage increases could lead to wage increases without disemployment effects. Most studies of monopsony use natural experiments focused on distinct localized labor markets or occupations (see Ransom & Sims, 2010; Staiger, Spetz, & Phibbs, 2010). Focusing specifically on the restaurant industry and using data from the Quarterly Workforce Indicators (QWI), Dube, Lester, and Reich (2013) directly test the impact of minimum wage increases on labor market flows, finding sharp declines in turnover rates without significant changes in employment levels. While this work provides convincing empirical support for the monopsonistic view of the labor market, there is still uncertainty as to how such mandates shape broader aspects of employment practices within firms. While this careful, cross-border quantitative research is important, these studies alone do not fully capture the motivations of firms or their explicit behavioral responses to policy changes. This paper seeks to test the major predictions of how firms in a monopsonistic labor market actively re-shape the employment relationship in response to binding local labor standards such as the minimum wage and health care mandates.

The reliance on monopsony models to explain the basic finding of small or insignificant disemployment effects in empirical research on the impact of minimum wage is also theoretically consistent with non-orthodox labor market theories based on the work of institutional economists. Beginning with work by scholars including Doeringer and Piore (1971) and Kotz, McDonough and Reich (1994) and others presented a descriptive model of the labor market (e.g. dual labor markets, labor market segmentation) which sought to explain structural inequalities such as persistent racial discrimination and job quality differences across and within industries through an analysis of institutions rather than individual agents. Consistent across all of these institutional accounts of the labor market is the observation that social norms and contexts matter and that employers have considerable power over wage setting and structuring the core aspects of the employment relationship (see also Peck, 1996; Tilly & Tilly, 1998). Paul Osterman (1999) uses a similar institutional lens to describe the major structural changes in the American labor market over the last half of the 20th century. The institutional approach is also used by scholars who document variation in labor practices and restructuring within certain industries (Appelbaum & Batt, 1994; Carre & Tilly, 2008). These scholars have consistently documented the existence of “high-road” employment practices—often associated with higher wages, benefits, training, and greater full-time employment—alongside a set of employers who pursue a “low-road” strategy aimed solely at lowering labor costs. This paper also relies on these institutional perspectives in developing hypotheses of how employers in the restaurant industry are likely to adapt to raising labor standards in

their local labor markets.

2.2 Existing research on Employment Practices in the Restaurant Industry

Although there has been no other study that attempts to test the implications of the monopsony model and related institutional labor market theories within the restaurant industry, a body of recent research documents employment conditions in restaurants. Specifically, research conducted by Restaurant Opportunity Centers (ROC) United and affiliated scholars provides new evidence on wages, benefits, working conditions, the extent of racial and gender discrimination, and variation in employer practices. In 2011, ROC released a study conducted in eight large metropolitan regions that consisted of surveys and interviews with both employees and employers that documented the prevalence of low wages, lack of access to health benefits and sick leave, and persistent occupational segmentation by race (United, 2011). More recently, Batt, Lee and Lakhani (2014) presented results based on a national employer survey across 33 large metropolitan areas focused on variation in human resource practices across restaurant market segments. They find a clear link between higher quality human resource (HR) practices and lower turnover. In a related study Batt (2012) highlights case studies of restaurants that pursue what they call “high-road” practices which include higher relative wages, more full-time work, and more investment in training.

While this growing body of research is crucial for better understanding the nature of employment in the restaurant industry, it does not explicitly analyze the role of labor standard mandates on outcomes. This paper complements this work by concentrating employer surveys and interviews on two cases that vary widely in the scope and magnitude of labor standards.

2.3 Hypothesis building: How labor standards might alter the employment relationship.

Before turning to a discussion of the research methods, it is important to note how theories of monopsony and related institutional research on labor markets would explain the impact of raising labor standards on employment outcomes. These theoretical implications form the basic hypotheses that will be explored in the empirical analysis proposed below.

First, by raising wage floors, minimum wage and living wage mandates are predicted to compress the distribution of wages offered within the industry. This effectively reduces the monopsony power of firms as they have a narrower range over which to choose an optimal wage/turnover combination. Thus, a key implication of this compression is the hypothesis that in the absence of high labor standards, firms in North Carolina’s Research Triangle region—where there are no locally enacted labor standards—will

engage in a wider variety of employment practices with starker contrasts between low-road employers that are very low (e.g. low wages, high turnover) and some high-road employers that can truly have their pick of the available workforce. We would expect the opposite to be true in San Francisco where a higher wage floor is predicted to result in the convergence of employment practices. In the latter environment, it is still possible that firms find non-wage outcomes with which to compete for workers. This is an area of inquiry that is best explored in detail through interviews.

Second, the (dynamic) monopsony model implies that as wages and other benefits rise through mandates, turnover falls accordingly. In fact, there is already empirical evidence that shows this to be the case (Dube, Lester & Reich 2013). However, this would also imply that firms operating in a labor market without strong mandates are more likely to hire workers from unemployment. The implications of this at the level of an individual restaurant are that for firms in San Francisco, lower turnover results in more workers staying on the job longer and, conversely, a higher share of new-to-the industry workers hired in RTP. Thus, I expect that firms will require more industry-specific experience when hiring in San Francisco, compared to RTP and a parallel finding of large differences in turnover. This hypothesis is explored directly through a survey of and interviews with restaurant managers who were asked to describe their recruitment strategy, how they seek their "ideal" candidates, and how they address challenges in finding skilled workers in each occupational category. This qualitative approach will also provide insight on differences in the norms and expectations employers have of their workforce and highlight how skills are framed and sought after in the hiring decision.

Third, by reducing turnover and, by extension, raising average tenure levels within each firm, higher labor standards may also have an impact on the incentive to offer additional training to new workers, and perhaps, to create formal or informal internal job ladders. Since a higher hourly wage raises the marginal cost of each additional worker—in a monopsonistic setting—an employer may have a stronger incentive to extract productivity from each new worker and thus has an incentive to provide more training (Arulampalam, Booth, & Bryan, 2004). In particular, when the wage rate is high, the potential productivity gap between a new worker and the rest of a more experienced workforce is higher. A corollary to this hypothesis is that employers in a labor market with high labor standards will make less frequent use of part-time shifts since part-time workers require a longer period of time to gain experience and ultimately achieve higher productivity. However, there is ambiguity in the literature about the effect of higher minimum wage levels on training, as Rosen (1972) points out firms may attempt to offset higher labor costs by cutting back on formal training programs. This paper uses qualitative data gleaned from interviews with restaurant managers to shed light on the training strategies selected by employers and to highlight the potential non-monetary costs of training.

3. Methodology

3.1 Comparative Case Design

As noted above, this study uses a primarily qualitative research design of the restaurant industry across two fundamentally different institutional settings. In San Francisco employers face the nation's highest minimum wage ($10.74 per hour rising to $15 by 2018), a pay-or-play health care mandate (up to $2.33 per hour), and paid sick leave requirements. In addition tipped workers must be paid the full minimum wage. In Research Triangle Park (RTP) region[4] there are no locally enacted labor standards. Thus, the effective wage in San Francisco is over $13.00 per hour (Jacobs, Reich and Deitz, 2014) during the study period of January through October 2014.[5] Conversely, firms in the RTP region are bound only by the federal standards of a $7.25 minimum wage and $2.13 per hour for tipped workers, with no paid sick leave or health care spending mandate.

The analysis focuses on the full service restaurant sector only. This sample restriction is applied for several reasons. First, limited service (i.e. fast-food) establishments are more likely to have less flexibility in adapting to labor mandates as they tend to be less labor intensive, thus leaving less variation to observe. In addition, a key difference in wage regulations between the comparative cases is in the tipped minimum wage, resulting in more potentially observable treatment effects among full service restaurants. Lastly, fast-food establishments are more likely to be part of corporate franchise chains than full service establishments. Since many HR practices are influenced at a corporate level, it would be harder to attribute observed differences in fast-food establishments to local labor mandates rather than exogenous corporate policy. For these reasons, this paper focuses on full service restaurants.

3.2 Case Selection Methodology

While the regional labor markets of these two cases differ on a number of dimensions beyond the strength of local labor standards, there are a number of similarities that make this comparison plausible for detecting causal effects of labor standards. First, both regions are home to many high-tech employers and both have comparably tight overall labor markets. Lastly, both cases have a similar number of full service restaurant establishments, resulting in a similarly sized sampling universe.

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[4] The RTP region is defined here as the three county area of Wake, Durham, and Orange Counties in North Carolina.

[5] San Francisco voters approved Proposition J on November 4th, 2014, which raises the minimum wage to $12.00 on January 2015 and ultimately to $15 per hour by July 1st 2018.

3.3 Research Questions and Outcomes of Interest

As the goal of this research is to add richness to the empirical literature on monopsony in the low-wage labor market, the major hypotheses tested will follow directly from the dynamic monopsony and institutional models discussed above. Specifically, this paper tests the claim that variation in employment practices—as evidenced by variation in wage rates, turnover rates, benefits offered and non-wage compensation—will be greater in the RTP region since San Francisco's labor standards are predicted to compress the wage distribution. In addition, this project seeks to measure the degree to which employers in San Francisco decide to make stronger "investments" in their workers—through more careful searching, training, and using more full-time workers—as the monopsony and related institutional models predict. Lastly, by examining their behavior and reflections directly, this paper will assess the degree to which employers seek to redefine job roles, change job expectations, and ultimately reshape the employment relationship in the face of labor mandates.

3.4 Interview and Survey Methods

The main data collection method for this project consisted of a set of semi-structured interviews with approximately 15 employers in each case. The interview subjects were restaurant owners, general managers, or other key staff who have direct control or influence over the firm's human resource strategy. Subjects were solicited from and represent all major restaurant market segments (e.g. family-style, casual fine dining, and fine dining), offering a range of observations according to price point and revenue. Interview subjects were initially solicited via a web-based survey (described below) inquiring about the willingness of survey participants to participate in a 45-minute interview. Additional interview subjects were solicited through phone calls and in-person requests by the investigator and a graduate student researcher during business hours. Subjects were compensated with a $50 gift card for participation. All interviews were recorded on digital media and transcribed for subsequent analysis.

This qualitative data collection is used to analyze how employers actively and uniquely construct their labor market practices in the face of institutional constraints such as wage mandates and prevailing industry norms. The interviews go beyond the survey results and seek to ascertain why a reported practice (e.g. training investment) was chosen.

In addition to the interviews, a web-based survey was conducted between July 1st and August 31st 2014 and collected a total of 104 valid responses. The survey consisted of 15 questions and was intended to gather detailed information on wage levels by occupation, training provided, skill requirements and educational attainment of workers. In addition the survey gathered background information on each

restaurant such as market segment, average entrée price level, and number of seats available. Table 1 below summarizes the number of respondents in each case by major market segment.

Table 1. Summary Statistics from Employer Survey and Case Industries.

	RTP		SF	
Restaurant market segment	**#**	**%**	**#**	**%**
Casual fine dining	17	34%	23	43%
Diner/luncheonette	3	6%	8	15%
Moderately-priced family style	18	36%	10	19%
Other	5	10%	5	9%
Upscale fine dining	7	14%	8	15%
Total valid survey responses	50		54	
Universe comparison.				
Total full service restaurants	1,703		2,349	
Total population (2013 estimate)	1,402,774		837,442	

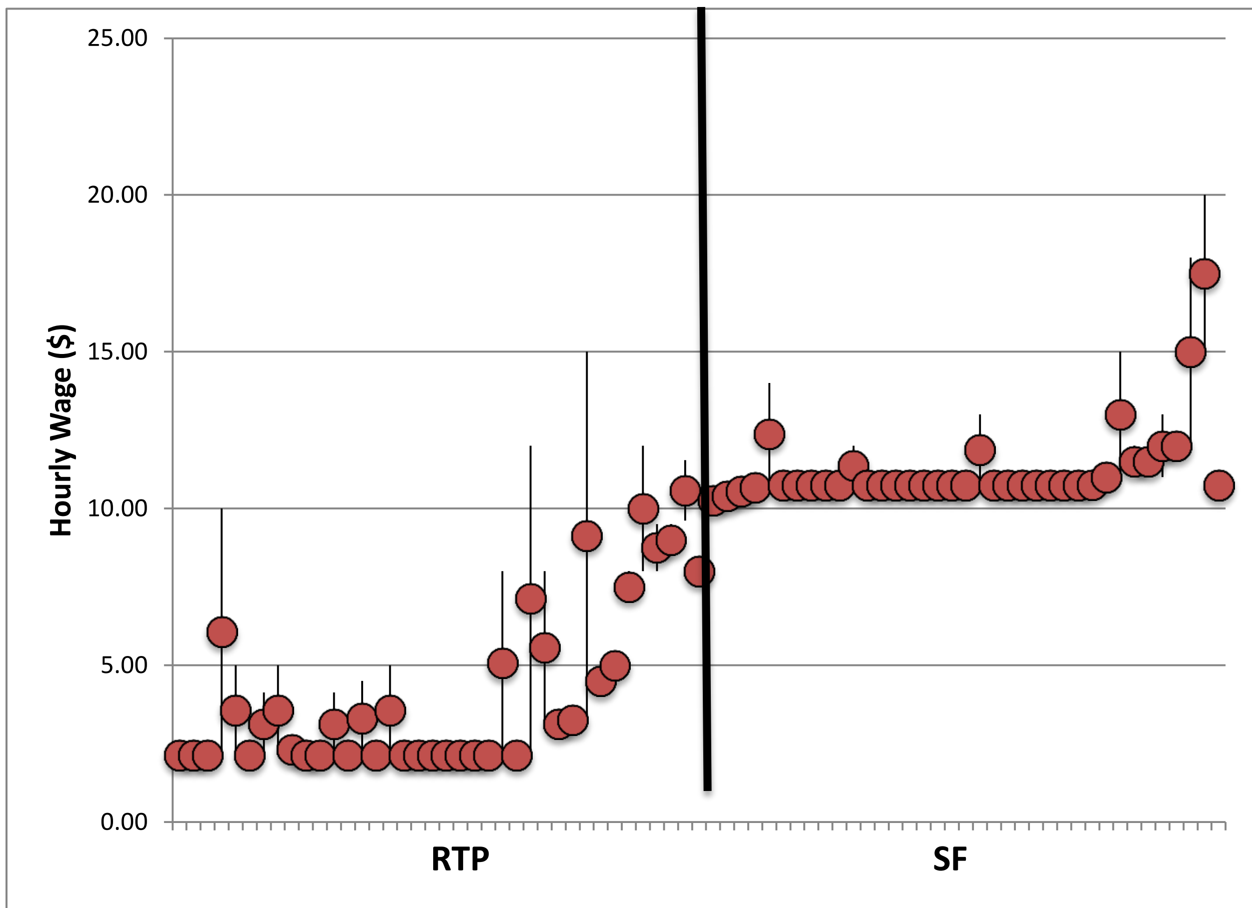
Source: Author's Analysis of Original Employer Survey of Full Service Restaurants in San Francisco and the RTP Region (N=104), Fall 2014.

4. Findings

4.1 Taking Away the Low-Road and Shifting the High Road Higher

One of the key predictions of the monopsony model is that raising the minimum wage will reduce existing wage variation within a given labor market as some employers who, without such a wage floor, would offer a lower wage and accept higher turnover while others would offer a higher wage and face lower quit rates. As such, a high and binding minimum wage and related labor standards would lead to wage compression and a general convergence of employer practices. Thus, raising labor standards can be interpreted as "taking away the low-road." This claim is directly observed from the survey data. Figure 1 below illustrates that wage variation for servers is indeed greater in the RTP region than San Francisco.

Figure 1. High, Low and Average Wage Rates for Servers in Full Service Restaurants in the RTP region and San Francisco.



Source: Author's survey of full service restaurants in the Research Triangle Park region and San Francisco (N=104). Bars indicate the range of wage offers (low to high) and points indicate the mean wage offer.

A visual comparison of the wage distributions above reveals that while most establishments pay servers the respective mandated minimums of $2.13 per hour in RTP and $10.74 per hour in San Francisco, there is considerably more variation in the RTP cases. Specifically, 57 percent of respondents in RTP reported paying at least one of their servers a wage above $2.13 per hour, compared to just 38 percent in San Francisco. Since the survey asked about the wages offered to the lowest-paid (i.e. newly hired) worker as well as the highest paid workers, we can compute the same comparison of wage offer rates for new workers. In RTP, 32 percent of employers offered a starting wage for servers above the mandated minimum, compared to only 21 percent of restaurants in San Francisco. Table 2 summarizes the wages offered by various occupations and presents the overall level of variance both across and within firms for each region. Overall, the wage variation is greater for RTP in nearly all occupations, as indicated by the standard deviation listed below each mean value. For example, the standard deviation was $2.14 for servers starting wage in RTP versus $0.88 for San Francisco. While these statistics capture the degree of wage variation measured across the industry as a whole, we can also observe the within-firm

wage variation by calculating the difference between the highest and lowest paid worker in each occupational category. Consistent with the industry-wide figures, employers in RTP offered a wider range of wages to their workers compared to employers in San Francisco. This difference in intra-firm wage variation was statistically significant for servers and line cooks. This survey evidence suggests that labor mandates—particularly the high and binding local minimum wage—are associated with less wage variation both within and across firms in the full service restaurant industry. Thus local mandates seem to "take away the low-road" by limiting the room that employers have to behave in a monopsonistic manner.

Table 2. Mean Wage rates by Occupation and Staffing Levels in Full Service Restaurants, Research Triangle Park (RTP) Region and San Francisco

WAGE RATES BY OCCUPATION	RTP-REGION	SAN FRANCISCO	D.O.M. SIG. LEVEL
Servers			
Lowest wage	3.21	10.80	***
	(2.14)	(0.88)	
Highest wage	5.23	11.64	***
	(3.83)	(2.20)	
Intra-firm wage range	2.00	0.79	**
	(3.07)	(1.56)	
Line cooks			
Lowest	9.09	12.50	**
	(1.48)	(1.55)	
Highest	12.27	14.93	**
	(2.66)	(2.36)	
Intra-firm wage range	3.18	2.43	*
	(2.30)	(1.93)	
Dishwasher			
Lowest	8.28	11.01	***
	(1.00)	(0.81)	
Highest	9.47	11.86	***
	(1.65)	(1.29)	
Intra-firm wage range	1.22	0.85	
	(1.35)	(1.08)	
Productivity Measures			
Total seats	142.0	94.2	***
	(105.28)	(75.60)	
Total servers	16.5	12.4	**
	(16.40)	(10.52)	
Sales per employee	47,082	68,206	***

Notes: Mean values for wage rates and staffing levels drawn from author's survey of full service restaurants (N=104). Standard deviations are listed below mean in parenthesis. Sales figures per employee calculated from records Reference USA drawn for

selected counties. D.O.M stands for difference of means and lists the significance level (p-value) from a simple T-test between regions. *** is significant at the 1% level, ** at the 5% level and * at the 10% level.

The survey also allows us to address differences in the size of restaurant and overall staffing levels across the cases. The average restaurant size is significantly smaller in San Francisco (94.2 versus 142.0 seats) and, as such, there were fewer servers employed in each establishment. However, this allows only a marginal comparison of worker productivity as size differences are more likely due to land costs rather than an adaptation to labor standards. A more direct comparison of productivity differences can be made by looking directly at reported sales per employee at the establishment level as reported in the Reference USA business listing service. Full service restaurants in San Francisco reported significantly higher sales per employee in 2014, $68,206 compared to $47,082 in the RTP region.

While the differences in wage variation between the RTP region and San Francisco—both within firms and across the industry—support the claim that labor standards are effective in raising standards in the low-end of the labor market, interview data reveals evidence that such standards also push some employers to go above the new standards. This is particularly evident in how some employers reacted to the enactment of San Francisco's pay-or-play health care mandate. Rather than requiring employers to provide insurance directly to workers, the San Francisco Healthy Families Act (2007) requires employers to pay up to $2.33 per hour worked for each employee. These payments can go either directly to the county health system—where resident workers can receive low-cost care—or into a separate health care spending account set up for each worker. This mandate involves a significant but uniform cost increase for all employers in the industry. However, in the face of this mandate, some employers decided to spend more than the mandated minimum in order to provide actual employer subsidized health insurance to all workers, a benefit that is extremely rare in the industry (ROC 2014). As one employer described:

> This year for example, we did employee health insurance for everyone... Now everyone has real insurance, not just the city thing. We think and hope it will help retain employees.—*mid-scale convention center restaurant manager.*

Another employer echoed the logic of providing full employers sponsored health insurance, rather than simply paying the lower cost option of a per hour fee to the City of San Francisco. The manager of one neighborhood-based fine dining restaurant explained:

> Part of our decision to offer health care goes beyond a simple cost-benefit—what's another thousand dollars if you already have to spend a certain amount of money. There is a kind of revolutionary like revolt thing happening in that I'm not going to just sign a check over to the city. I'm going to actually give it to my employees. And then the other part is it becomes part of your hiring and your attraction is that you say hey, we offer full benefits.—*neighborhood fine dining manager.*

Although this manager's initial sentiment reflects animosity towards the City for enacting the

Healthy Families law in the first place, the employer's actual behavior in paying more for full insurance indicates how the labor standard induced the employer to go above the minimum and embrace the potential retention and morale benefits for their workforce.

Beyond direct wage and benefit offers, we can observe how employers in San Francisco reshape other aspects of the employment relationship in an effort to differentiate themselves from other employers in the market and to ultimately retain valued employees. Several interview subjects discussed how they attempt to create a unique work "culture" that is "exciting," "fun," or offers indirect benefits to workers, even in cases where employers cannot raise wages beyond the mandated level. For example, an owner-manager of a small neighborhood casual restaurant describes how he allows line cooks to use the resources of the restaurant to further their career development and pursue income generating work as part-time caterers.

> [Although we can't always compete for line cooks on wages alone], we're not as always regimented and stuffy [as other kitchens], we have a lot of perks. If someone needs to do a private party and they need something from us, sometimes we will offer some of that product that they need or let them work here in our space. And if they need their spices or other things, usually people pay us back if they like. There are a lot of cooks that do work on the side too…So they'll use our kitchen space, or we'll let them order stuff, bring them in on an invoice at our wholesale rate and they can pay us back on that and we usually don't mark that up. It's not something that we discourage, no, I mean it's learning and it's something that we can provide—we can't pay everyone 15 dollars an hour, I wish we could, wish we could pay them more.—*neighborhood casual restaurant manager.*

Another employer described their efforts to retain key workers in lower-paid occupations through the use of in-kind compensation that is matched to the specific needs of the individual worker.

> Through working with everyone on a daily basis we try to keep everyone happy and in a good mood, you know. [For example] we just started doing an employee of the month program but not in a traditional McDonald's kind of way. Our dishwasher that's been with us for five years and we never want to lose him. He's from Mexico and his family's all back there so we bought him-- and we did a presentation in front of all the staff and gave him calling cards so he can call his family more frequently, whenever he wants. And we actually just gave [a backwaiter] the employee of the month today and since his daughter is having a quinceañera party coming up, we offered to host all of the alcohol for that party and have it here.—*mid-scale convention center restaurant manager.*

While these may seem like relatively minor gestures on the part of some employers, these forms of non-wage compensation represent additional ways in which we can observe the tendency hypothesized by the monopsonistic model and institutional theories of the labor market for employers to differentiate themselves in order to retain workers. In the face of strong, binding labor standards that effectively limit the degree to which this differentiation takes place via the wage (i.e. "taking away the low-road"), we still observe differentiation in how employers structure the employment relationship. In these two examples we observe restauranteurs who—perhaps implicitly—are adopting some of the same progressive human resource practices typically associated only within high-skill industries or occupations. Specifically, they

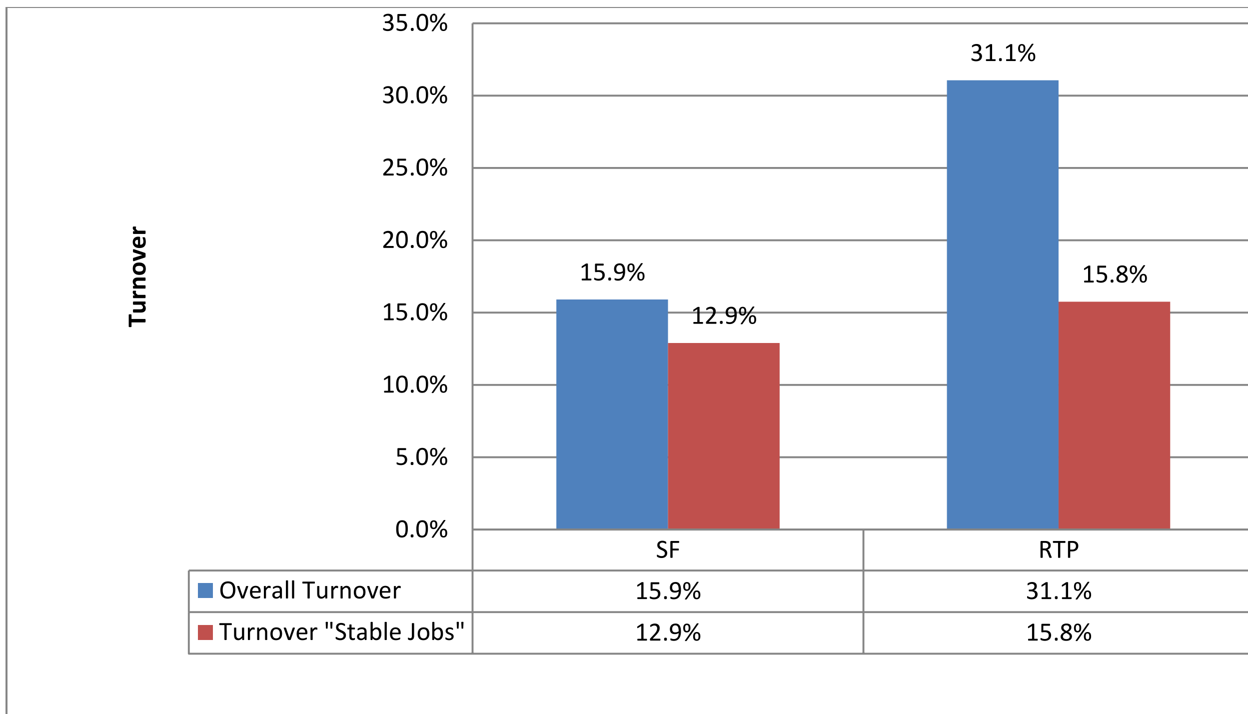
are recognizing and seeking to accommodate the individual needs of each worker, whether that relates to the worker's need for outside income through catering or in-kind support of family obligations.

4.2 Stronger Matches and the Rise of Professional Norms

The greater degree of wage variation observed in the restaurant industry in the RTP region compared to San Francisco is broadly consistent with the narrative explanation offered by both the monopsonistic and institutional understandings of how higher labor standards impact the labor market. Parallel to this observation, we also find evidence that higher labor standards lead to stronger, longer-lasting matches between employers and workers. This finding is borne out by evidence from a variety of sources including publicly available employment statistics on labor turnover, original survey results on employer hiring expectations and requirements, as well as interviews with employers themselves. Beyond the direct finding that raising wages and benefit standards reduces turnover, the qualitative evidence drawn from employers indicates that higher labor standards may have deeper impacts on the prevailing norms and expectations in the restaurant industry. Specifically, employers in San Francisco readily describe their ideal employees in language that describe worker traits and behaviors that are typically used to describe *professionals*—meaning workers who have recognizable industry-specific skills, typically work full time, and invest in their own training.

The rate of turnover for the overall full service restaurant industry in San Francisco was 15.9% in 2012, according to official statistics from the Quarterly Workforce Indicators (QWI) program. This compares to 31.1% in the RTP region. However, as seen in Figure 2 below, this stark contrast in turnover is largely due to the relatively high rate of short-term workers who enter and exit employment at a given firm within the same quarter. The difference in turnover rate for "stable" jobs—meaning jobs that last more than one quarter—is much lower (12.9 versus 15.8%). This means that the full service restaurant sector in RTP features a significantly higher number of unsuccessful, or weaker matches than San Francisco's restaurant sector.

Figure 2. Labor Turnover Rate for Stable Jobs and Overall Jobs in the Full Service Restaurant Industry in San Francisco and the RTP Region, 2012.



	SF	RTP
Overall Turnover	15.9%	31.1%
Turnover "Stable Jobs"	12.9%	15.8%

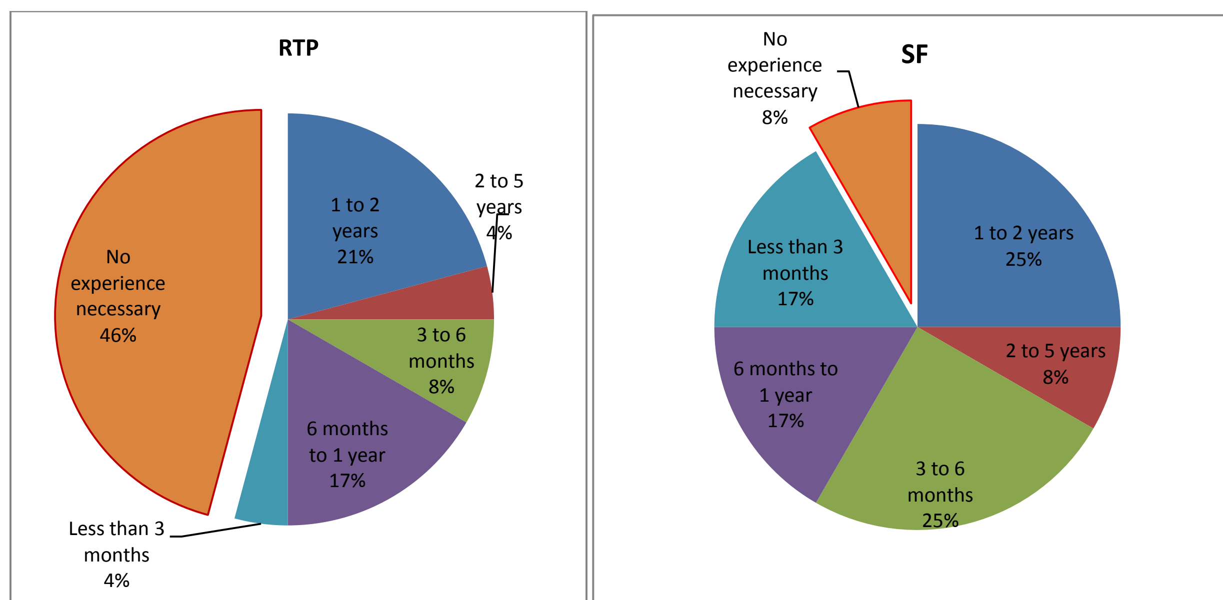
Source: U.S. Census Bureau. 2012. Quarterly Workforce Indicators Data. Longitudinal-Employer Household Dynamics Program http://lehd.ces.census.gov/data/#qwi.

These very short term jobs—lasting less than one quarter—are often described by labor economists and other observers as evidence of bad matches between employee and employer (Barlevy, 2002; Gautier, Teulings, & Van Vuuren, 2010). The prevalence of these low-quality matches are indicative of labor market conditions in the restaurant industry that feature a large number of potential workers flowing into and out of employment. While the QWI data do not allow us to observe exactly why a worker left a job, the most common mechanisms include a) quitting to take a better job in the industry or similar industry, b) quitting a job and exiting the labor market, or c) being fired by the employer. In a low-wage labor market without binding labor standards, we would expect all of these exit mechanisms to be more pronounced as the wider wage variation would induce workers to change jobs more frequently, and as the relatively low industry-wide wage would be closer to more workers' reservation wage. Finally, as I argue below, lower-wage labor markets without binding standards engender weaker expectations of worker quality on the part of employers which leads to a lower bar for entry and ultimately more firing of low-quality workers.

To address these explanations of contrasting labor market conditions between regulated (San Francisco) and unregulated labor markets (RTP), we need to move beyond the high-level snapshot provided by the turnover figures. Specifically, we need to directly examine the kinds of matches that occur in the restaurant labor market and search strategies that employers use to generate them. First, the

restaurant industry in RTP tends to hire younger workers with a lower level of formal education. Specifically, 49.5 percent of workers in RTP are under age 24 or have less than a high school education, compared to 38.9 percent in San Francisco. Conversely, 40.6 percent of workers in San Francisco have some college or a bachelor's degree or higher, compared to 29.7 percent in RTP.[6] While these differences could reflect differences in labor supply available in these two settings, they are greater than the overall differences in educational attainment across the entire labor market.

Figure 3. Minimum Experience Required for Servers in the RTP and San Francisco Full Service Restaurant Industry.



Source: Original Restaurant Employer Survey (N=102), conducted Fall 2014.

In addition to hiring an older and more educated workforce, San Francisco employers generally engage in more careful searches, which lead to overall better matches. First, employers in San Francisco report higher experience requirements for new hires across the occupational spectrum. As seen in Figure 3, only 8 percent of survey respondents in San Francisco reported that new servers could be hired without any previous experience in the restaurant industry, compared to 46 percent in RTP. Also, a larger proportion of the San Francisco employers reported experience requirements of over one year—33 percent in San Francisco, compared to 25 percent in RTP. The lower bar for entry into employment is also confirmed in employer interviews. For example, one RTP manager explained what he looks for in a new front-of-house worker as follows:

Basically, we require [that a server] can work a four shift minimum per week and go an entire shift, an

[6] Quarterly Workforce Indicators, 2012Q3.

> entire eight hour shift without smoking a cigarette and [without] any facial piercings or anything. Beyond that, just come in with a smile on your face.—*neighborhood bistro manager in Raleigh.*

Survey and interview data indicate that employers in RTP place less value on industry-specific experience. Yet even in firms that do prefer experienced workers, managers and owners did not articulate how experience matters or which specific skills or demonstrated industry-specific knowledge they require. As one manager describes:

> We look for at least one year's experience, but the biggest thing we look for is we look for the person. We don't look for the skill. I could teach anybody how [to] wait tables [and] pour drinks. I can teach anybody how to cook steaks. What I can't teach is how to be a good person.—*upscale bar and grille manager in Raleigh.*

Employers in San Francisco discussed the minimum level of experience needed to work in front-of-house positions in a distinctly different tone. Rather than viewing servers as essentially interchangeable laborers who can be trained quickly and easily if they possess a modicum of personal hygiene and a friendly personality, employers in San Francisco exhibited a clear description of what a "professional server" was and the explicit and implicit skills required. One employer described her front-of-house staff as follows:

> We have a lot of people who have made it a career and they're investing in the knowledge of the product and learning their trade or already know their trade because they've done it for years.—*mid-scale restaurant manager in San Francisco.*

Another San Francisco owner described the level and nature of experience needed to fill a server position in his neighborhood bistro.

> Realistically, to work here, I would say [a server needs] five years of experience, because there's a wine knowledge level that I expect that you really just couldn't get any other way....If you have ten years of experience at Applebee's, that doesn't do anything for me.—*neighborhood bistro owner.*

The fact that this employer is seeking a candidate not with just time on the job at any restaurant, but rather a similar kind of full service restaurant is a point that was echoed by many employers. Thus employers care not only about how much time a worker has spent on the job, but where that job took place, and how much time was spent there. As one manager put it, "I look also at loyalty. How long were they at a certain place? So if they worked at a good restaurant, and they were there three years, they must be doing something right." Many employers also stressed the importance of working in restaurants in San Francisco or other cities with a well-known restaurant culture (e.g. New York). Ultimately these responses indicate that employers are looking carefully down each candidates' resume and approaching the hiring process with a set of expectations about the nature of work, the skills (e.g. how to manage a customer's dining experience rather than take orders), and industry-specific knowledge needed to perform at a high level. Compared to employers in RTP, these San Francisco employers tend to view their

employees—front-of-house more so than back-of-house—*as professionals* rather than basic labor inputs.

This rise of professional norms—or the exhibited expectations of employers for certain worker traits that are typically associated with highly trained professionals—can also be seen in the unexpected finding on employer-provided training. One of the key implications from the work of labor market theorists who argue that employer practices are flexible, is that high-road employers will spend more resources on training. Their low-road counterparts expect their low-wage workers to quit and their low-wage workers seem easily replaceable. This makes sense in industries like manufacturing where this insight was first observed (Appelbaum, 2000). However, this research finds that in fact the opposite is true. San Francisco employers reported spending less time offering formal training periods for both front-of-house and back-of-house staff. Instead, they seek out and expect to find workers who already possess a high level of skills in the industry.

One San Francisco employer remarked: "I have to invest too much. To bring you even from an experienced waiter into being one of our waiters costs me too much money to work with people that aren't going to be around for a while." This response not only indicates an employment screening process that seeks workers who want to work full-time and do not have competing demands on their time (e.g. school enrollment), but also a high degree of firm-specific knowledge that must be gained only by on-the-job training.

In contrast, more employers in RTP discussed a recruitment and training model that were more likely to involve formal screening mechanisms for a high volume of applications and a longer, more formal training period for new hires (particularly for front-of-house workers). These training strategies are maintained to deal with the high level of labor turnover and the reliance on relatively less skilled workers. For example, the manager of a large sports bar and grill in RTP explained the recruitment and training process as follows.

> [We have a front of house staff of 75 to 80 at any one time] You know, a lot of recruiting we do online through Craig's List. We're doing a Zip Recruiter. There's some websites that we go through our office, they send out all that stuff. We do all of our applications online. When people come in, we don't physically hand them a piece of paper. We hand them a card. It tells them what website to go on. They go ahead and take an assessment. The assessment is scored, and then we get all those almost instantly. This web-based system pulls all the information up on a Manpower Plan, it tells us what they've applied for, where they've worked. Gives us a resume, and then it gives us a score on the assessment. — *neighborhood family dining manager.*

Once an employee is hired, they enter into a formal training period that is standardized for each occupation.

> Training is a huge investment for us and it is constant. We're going to have a training class here, in a minute. Since it happens every Tuesday from three thirty to four thirty. Training days depend on the position. Bartending training is 10 days and servers require 8. In the kitchen it's probably about 10 days.

> Every day they write note cards on all their recipes. But they'll take a final. When they take their final, their test in the kitchen, they have to know every ingredient, every ounce, and every item, for the entire station. That's why we require them to write note cards.—*neighborhood family dining manager.*

In RTP, even at higher-end restaurants, employers have built a human resource system that accepts a high rate of turnover. As one employer explains:

> Well, we try to stay ahead of the game so that we're always hiring, we're always interviewing, but hopefully it's not desperation hires. Hopefully-- and we try to-- so we have between 25 to 40 servers at any point. And we try to have a mix of needs like people who need fulltime, who can work lunches and brunches and all of that, to servers who really want very part time so that you can kind of over staff on busy shifts and then there's always someone that wants to go home. There's always a student that would like a Saturday night off.—*casual fine dining manager in Raleigh*.

Rather than engaging in formal training programs during work hours, the overall higher level of expectation on the part of San Francisco employers that their workers have "professional norms" translates into efforts to support continuous skill upgrading and quasi-professional development activities that are integrated into the jobs themselves. For example, one employer described that in addition to limited initial training on their internal systems for servers, the restaurant has designed a system to support ongoing knowledge development.

> Sometimes we'll assign different topics like rum to one person and then they come back and they're responsible for training everyone else, doing kind of an in service just to keep it interesting, keep them motivated to learn. If they're having to present it to someone else, they're going to want to know the product. It's sort of a team approach, you would use the whole team to train the rest of the team. Next week somebody gets vodka, next week somebody gets some small winery up in Napa. And we don't just do products, sometimes we'll do a certain vegetable, they have to find out the history of it.—*casual fine dining restaurant manager*.

Another San Francisco employer explained that the opportunity to learn on the job actually becomes a recruiting and retention tool for his staff.

> The attraction of working here is that they get to taste a lot of wines. It's a big wine list. They can kind of flex their wine muscles a little bit and be like kind of like mini-sommeliers on the floor. They don't hand over all the wine sales decisions to me or someone else. They handle it themselves.…We've had no turnover for two years.—*neighborhood bistro owner*.

Overall, compared to respondents in RTP, San Francisco employers were less likely to report lengthy formal training periods for either front-of-house or back-of-house workers. Instead, there is an overall higher level of skill expectation and—as is the case for many professions—workers are expected to acquire and exhibit industry-specific knowledge on their own. While it is difficult to ascribe the divergence in employer norms to higher labor standards alone, efficiency wage theory suggests that as labor costs increase employers have a greater incentive to extract more productivity from each worker. Instead of manifesting itself in work intensification or greater scrutiny on the part of managers, San

Francisco employers seem to be seeking out better trained, more experienced workers and expecting more from them.

4.3 Labor Standards and the Restructuring of Work: Limitations and Innovations

The previous sections of this paper documented the differences between the employment practices in the RTP region and San Francisco regarding the overall wage distribution, workforce characteristics, and professional norms and expectations, and tied those findings to the distinct institutional environments. It is also important to understand both the potential limitations of labor mandates in addressing ongoing inequality in the industry and how some employers have adapted by fundamentally altering the compensation model.

An important caveat to the claim that higher labor standards have engendered greater professional norms in the industry is that these norms and expectations are more prevalent for front-of-house workers than back-of-house workers. Employers in San Francisco increasingly treat servers as "professionals" and rely on resumes and demonstrable knowledge and previous local experience when hiring. Yet employers in both the RTP region and San Francisco still view back-of-house workers (line cooks, prep cooks, dishwashers) in a less formal, more racialized frame. For example, the manager of a corporate chain restaurant in Chapel Hill—who also previously managed several independent restaurants in the region—described the large Latino workforce in kitchens as follows.

> The Latino workforce, these guys know how to work. They've been typically cooking in their own kitchens for large extended families. This is how they typically grew up. So it's not like me cooking for a family of four at my house, or a family of five, or even doing a Thanksgiving dinner for maybe nine people. They're cooking three meals a day or whatever it is, for their extended family or for many people in the household. I think that's where a lot of those skills come into it just based on how they grew up. Compared to those workers with formal culinary education, I've probably kicked more people out of my kitchen who had a formal education, because they think they know everything now. It's one of those things where if somebody taught you how to cook eggs right, if somebody taught you how to do certain things right then that's wonderful, but can you actually get in that kitchen and perform and do multi tasks.—*moderately priced chain restaurant manager.*

The stated preference for Latino workers as prep cooks and line cooks undermines the utility of formal credentialing programs and codified skills that can be marketed across firms. The connection between ethnic background and perceived work ethic can lead to an assumption that Latino workers are monolithic and interchangeable. This ultimately limits the opportunities for individual workers to move up the pay scale. Furthermore, a large proportion of hiring is done through highly localized social networks that are dependent on the employers' own knowledge of other firms in the local industry. As one Durham restaurant owner—who previously cooked in a well-known area restaurant—explained:

> Everybody that we started with, our key players in the kitchen came from people that we knew from [a well-known Durham restaurant] that were leaving at the same time we did…When we needed extra help in

> the kitchen we hired our line cook's wife…our food runner is another cook's cousin's girlfriend….They're mostly Hispanic, new workers would come in and say: 'this is where I've cooked. You know so and so. That's why I'm here because she sent me here to talk to you.'—*Neighborhood fast casual restaurant manager in Durham*.

In San Francisco, employers also offered a view of back-of-house workers that emphasized ethnic stereotypes rather than formal skills or credentials.

> You know, a line cook position, I hate to say it, most of them are my people, most of them are Mexican. …And you know, you try to stay away from anyone who went to serious cooking school, went to a culinary academy, or has an AA in culinary kitchen skills… [Mexicans] are just a better quality cook, they really are. I hate to say it. They might not have-- they might not know what sous-vide is…but if you teach them once how to braise something, how to do it correctly, they'll do it better than the guy who went to school. It's just innate.—*Neighborhood ethnic restaurant manager.*

The equation of ethnic status with work ethic or "innate" ability may, on the one hand, lower barriers to entry for new workers to enter a back-of-house occupation. On the other hand however, the way employers frame skill through an ethnic lens reinforces the barrier between front-of-house and back-of-house workers. This barrier is important, not only because it limits access to better-paid server positions, but also because, as labor standards rise, this wage differential grows. There is a language barrier that may limit the ability for some workers to make the transition to the front-of-house positions, but employer views also reinforce the barrier. As several San Francisco respondents explained:

> That whole support staff, porters, dishwashers, all that, it's all Latin. I've never seen a white guy walk in here for that job, ever, in any restaurant I've been in ten, in eleven, twelve years. —*Neighborhood fine dining owner.*
>
> We have a lot of English-as-a-second-language staff members, and they're just not proficient enough to work on the floor—*Neighborhood casual restaurant manager.*
>
> I don't think there's a desire to move into – I don't think our folks have a desire to move into that position [server]. I think it's more of a, this may be isolated to us, but I feel like those folks are typically more introverted and would rather be the workforce behind the scenes.—*Convention center restaurant manager*

The barriers between back-of-house and front-of-house occupations is an observation that nearly all respondents in San Francisco brought up in response to direct questions about how they reacted to rising minimum wage and other labor standards. In particular, employers claim that higher labor standards exacerbates the difficulty they have in finding and retaining high-quality line cooks and prep workers. In their view, since the mandates require them to give raises across the board, including tipped workers whose total hourly income already exceeds the new mandate, they have less financial flexibility to offer higher wages to non-tipped workers. As one manager describes:

> From the back of the house and particularly cooking the line, somebody that needs some, not quite chef

> caliber but somebody who's just on production putting stuff out, that's super hard to find and mandates is a big reason for that because their pay scale hasn't risen in the same, can't rise in the same way that others have and it puts that strain on keeping them. So you're really looking for people that are capable but not quite as polished…And those folks are in short supply and there's a lot of competitive people looking for them. If you can cook the line well for under 15 bucks an hour then there's a lot of people that want you. —*Neighborhood casual restaurant manager.*

While this reaction was common among San Francisco employers, it is not clear that without the mandate, they would have paid their back-of-house workers more, or if the (market-based) competition for quality line cooks would result in rising wages since skills are viewed in very informal way. Despite the pressure that mandates put on employers, many still find a way to adapt by seeking productivity improvements, cross training of front-of-house staff, and raising prices.

There are a variety of ways that employers reported seeking higher productivity from staff including asking servers to do more "side work" such as cleaning, preparing for service for the next shift, restocking supplies and similar non-direct to customer interactions. Some employers discussed creating a tip-pool system that encourages all servers to provide service to all tables, rather than just their own. One employer in Raleigh described how the differential base-pay rate translates into greater work effort on the part of front-of-house staff.

> I think that when you're getting ten dollars and hour versus $2.13 you can ask for a lot more from a server. You know, I've had the $2.13 thing thrown in my face lots of times. It's slow. We're asking you to clean something. Somebody that's new to restaurants is like, 'I'm only getting 2.13 an hour, I shouldn't have to do that'…I know how much you make. Nobody gets $2.13 an hour. You're gonna walk out of here with 20 dollars an hour tonight, so you can't say that to me…If they were paid $10 per hour, that argument goes out the window…If the restaurant's paying you ten dollars an hour, they can pretty much ask me to do whatever, and I have to do it.—*Casual fine dining manager in downtown Raleigh*

A far more common reaction to higher labor standards has been to raise prices. Often, employers use a variety of mechanisms to hide price increases from customers by raising the price of common beverages, or appetizers. One employer in Raleigh explained how he would adjust to a higher minimum wage in the following manner.

> I mean, we give a pretty high level of service here. We're not going to put less people on the floor, because if you put less people on the floor and think you're going to grow sales, you're freaking crazy. [raising the minimum wage to $10.10 per hour] would mean, off the top of my head, another three and a half to four percent on the labor line. So we would dig into where we could find that three and a half percent just to keep our margins the same. [Here's an example of how we could do it.] We got a little bit of a niche on our beer. We sell Miller Lite for $5.50. That's a pint. You can go next door right now and get a 30 ounce bumper of Miller Lite for two bucks. The reason we do sell Miller Lite for $5.50 is because we'll sell Chimay at $7.00. We would find a way to adjust to the 3 or 4 percent overall increase in labor costs by doing some kind of cross subsidy like this. Take it out of high margin items.—*Manager at chain themed restaurant.*

While the response above indicates the level of flexibility some restaurants have in adapting to a higher minimum wage through clever price increases, in the case of San Francisco and other highly

competitive markets, raising menu prices has its limits. Instead, some employers have responded to mandates by adding surcharges to bills. The practice in San Francisco of adding surcharges—typically ranging from 2 to 4 percent—began after the 2006 San Francisco Healthy Families law took effect and was described by some respondents as a way of protesting the City's mandate. However, the practice quickly spread throughout the industry. Based on our employer survey, 50 percent (23/46 valid responses) of full service restaurants reported adding a surcharge, and 82 percent of these respondents (19/23) indicated that adding a surcharge did not change the typical amount that customers tipped. This indicates a willingness of customers—at least in San Francisco—to pay more when they know the added cost is going to workers.

Our employer survey also gives descriptive evidence about how employers have responded to all of collective labor mandates enacted since 2004. San Francisco full service restaurants that were open before 2004 were asked to rank various adjustment mechanisms in order from most important to least important for their experience. Table 3 below lists the mean rank score of each adjustment mechanism offered.

Table 3. Ranked Employer Adjustment Mechanism to Increased Labor Standards in San Francisco.

ADJUSTMENT MECHANISM	MEAN RANK	N
Raise prices	1.78	27
Reduce existing working hours	2.74	27
Increase worker productivity	3.96	26
Alter menu items to reduce food costs	3.96	26
Reduce hours of operation	5.08	26
Change the proportion of workers from front-of-house to back-of-house	5.35	26
Reduce other non-labor costs (utilities, marketing, etc.)	5.54	26
None of the above	7.50	26

Source: Original Restaurant Employer Survey (N=102), conducted Fall 2014.

The descriptive data in Table 3—while limited in scope—underscores the direct response from employer interviews and from the evidence on the widespread prevalence of surcharges (a form of price increase) in that price increases are the most common form of adjustment. The second most important factor, "reduce existing working hours" should be interpreted as more strict management of when workers clock in and out, rather than a true reduction in labor demand. As many managers explained, they have become more vigilant in making front-of-house workers clock out or go home early when business is slow, rather than an across-the-board reduction in the length of all workers' shifts. The next two options selected indicate the flexibility of employers in adapting to increased labor costs. While this quantitative

evidence is taken from a relatively small sample and should be interpreted with caution, they nonetheless provide context for the interviews.

The last and potentially most interesting way in which employers in the full service restaurant industry are responding to higher labor standards is through a radical restructuring of the compensation practices throughout the restaurant. Specifically, some employers are eliminating tipping and applying an across the board service charge (e.g. 18 or 20 percent) in order to redistribute income between front-of-house and back-of-house positions. The elimination of tips is a relatively rare business model in the U.S. restaurant sector but there have been a number of recent, high-profile examples that have accelerated the pace of change. For example, the nationally recognized restauranteur Danny Meyer, who owns several upscale restaurants in New York City (e.g. Gramercy Tavern, Union Square Café), announced that all of his New York-based restaurants would go "hospitality included" within a year. He specifically cited the need to rebalance the pay scale for kitchen staff after the recent increase in minimum wage for restaurant workers in New York.[7] The practice of including service either in the menu prices themselves or through a surcharge, while rare in the U.S., is the industry standard in many other countries including France. Some interview respondents in San Francisco gave unprompted support for this compensation model. The manager for multiple fine dining restaurants explained:

> If I opened a new restaurant tomorrow…I would 100% put everybody on salary. I would charge a flat percentage surcharge, and I would, I'd put everybody on salary…direct to customer employees probably start at $65,000 dollars a year and they cap out at $110,000 and non-direct to customer employees probably start at $45,000 and also would likely cap out at $110,000. And you know, you're eligible for raises annually based on performance, and then two bonus structures a year.—*fine dining manager.*

While the ability to raise prices or add significant surcharges in order to eliminate tipping may be limited to higher-priced restaurants, or very profitable establishments, it is clear that rising labor standards in cities like San Francisco and New York are accelerating this trend. One barrier to a more widespread adoption of this approach is the way payroll taxes are assessed. If a service charge is collected by the employer—rather than the employee in the case of tips—and paid to workers in salary or higher hourly wages, then the employer must pay additional payroll taxes into the unemployment system. Two additional interview subjects cited this added cost as a minor barrier to moving to a tip-less model. What is interesting about this recent restructuring of compensation practices is not that it will be immediately adopted throughout the industry, but that it illustrates that alternative business models are possible, including ones that focus on evening the playing field between front-of-house and back-of-house workers.

[7] Gordimer, Jeff "No Tipping, the Danny Meyer Way" *New York Times* (November 18th, 2015) p.D8.

5. Conclusion

The full service restaurant sector added 811,700 jobs nationally between June 2009—the official end of the Great Recession—and October 2015. This growth outpaced overall private sector job growth (18.1% versus 11.4%), and this trend is expected to continue as jobs in food service occupations are projected to grow faster than the overall labor market through 2030. Thus the restaurant sector is in many ways a useful harbinger for the predominant labor market conditions that policy makers can expect in the emerging service economy in the 21st century—namely the proliferation of low-wage jobs in place-bound service industries. Since the Great Recession, the most important policy response to this problem has been efforts to raise the minimum wage and other labor standards at the state and local level. Therefore, understanding how labor standards not only impact the pace of job creation, but also more general aspects of the employment relationship is critical. This research attempted to shed light on this question through an extreme case comparison of two labor markets which have starkly different labor standards and thus institutional environments. Rather than offering definitive causal evidence on their disemployment effects or strict bounds on a particular point estimate, the research offers a primarily qualitative narrative explanation of *how* local labor mandates influence employer behavior, realign incentives, and restructure job roles and expectations. As such this paper makes two key contributions, the first theoretical and the next empirical.

First, the findings of this paper—borne out of original survey data and employer interviews—are broadly consistent with a monopsonistic view of how local labor markets operate. Specifically, we found that the labor standards in San Francisco were associated with greater wage compression within occupations. More, workers were paid at the higher wage floor and employers had less "wiggle" room to offer slightly higher wages to attract workers and reduce turnover. Conversely the restaurant industry in the RTP region offered a wider ranges of wages—as some employers chose to pursue a low-road strategy while others offered wages above the mandated minimum. This finding also held within the firm as intra firm wage differentiation was also greater in the RTP region. However, the tendency for some employers to differentiate themselves to attract and retain workers was also evident in San Francisco, although it was pursued in non-wage aspects of the employment relationship. Thus mandates can be interpreted as both taking away the low-road and pushing the high-road higher. This finding would not make sense under the neoclassical theoretical viewpoint where firms are simply price takers on the wage for undifferentiated labor inputs.

Second, the empirical analysis suggests that higher labor standards have reshaped the employment relationship by: a) inducing employers to conduct more careful searches; and, b) making it more worthwhile for workers to stay longer in the positions the end up finding. This is borne out by the lower turnover figures—especially for jobs held less than one quarter—and by survey data showing

required experience levels for key occupations. Beyond these figures, the interviews illustrate that employers in San Francisco tend to use language that describes their front of house workers as professionals, thus reinforcing norms of worker skills and expectations that are not seen in to the same degree in the RTP region. The greater attachment between workers and firms in the restaurant industry under an institutional environment with higher labor standards can begin to produce some of the positive externalities of "high-road" labor practices described in other industries. Specifically, workers may become more productive—mastering firm-specific skills and having more experience—which may increase sales for owners and ultimately create better dining experiences for customers through better service. While the evidence produced in this two-case comparison is potentially limited and could benefit from looking at employment practices in other locales, it at least suggests that restaurant jobs are not in and of themselves a fixed category and that key aspects of the employment relationship and ultimately the structure of work within firms is malleable.

Lastly, it is important to recognize that there are limitations in how much local labor standards can impact job quality within the restaurant industry and more research is needed to fully assess the impact on overall wage inequality and opportunity structures more broadly. As indicated by the findings here, there remain deep divisions within restaurants between occupations (front of house versus back of house) and along racial and ethnic lines. Employers in San Francisco uniformly denounced the way minimum wage increases exacerbated extant wage gaps between servers and kitchen staff. While some employers have responded by adding service charges or, in a more radical response, eliminating tipping, it is too soon to tell how widespread these examples of restructuring will be.

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