Surviving Minumum-Wage Hikes at a Seattle Restaurant

By Galen Collins

Introduction

Amy's Café is an old-fashioned, home-style restaurant and bakery located in the heart of downtown Seattle. It has provided wholesome meals since 1959. In 2014, the Seattle city council voted to increase the city's minimum wage to $15 per hour in 2015, phasing in over a number of years. Increasing the minimum wage, a hotly debated topic, has been a priority of labor and worker advocacy groups throughout the United States. Many would argue that increasing the minimum wage boosts consumer spending and reduces income inequality in the economy. The National Restaurant Association, however, maintains that mandatory minimum-wage increases impose a significant financial burden on restaurant businesses. Amy McMillian, the owner of Amy's Café, is now concerned about the long-term viability and stability of her business. The case study scenario addresses different stakeholder perspectives on the minimum-wage issue and potential strategies for offsetting wage increases. It concludes with discussion questions and suggested readings to help the reader identify, reflect on, and assess various factors involved in the wage-hike dilemma facing Amy's Café. The purpose of this case study is to broaden the reader's critical thinking framework on possible measures for coping with mandatory minimum-wage increases in full-service restaurant environments.

Background Information

Among the lively and exciting new restaurants in Seattle, the old reliable spots are sometimes forgotten. Nevertheless, these restaurants have stood the test of time, making them classic dining spots that are quintessentially Seattle. Included in that list is Amy's Café, a 150-seat, full-service restaurant established in 1959. It is known for its fluffy omelets and healthy skillet dishes. Other menu items include soups, salads, and sandwiches. Everyday Amy's bakers prepare fresh baked gourmet breads and rolls.

Amy's café was started on a shoestring budget after the founder Amy McMillen stumbled upon a neglected 5,000 square-foot-space in the heart of downtown Seattle, Washington. Amy's interest in the food business began when she landed a job cooking at a basecamp in a remote wilderness of Washington. After a few short weeks at the camp, she had an epiphany that cooking was her passion and could lead to a successful and fulfilling restaurant career. The rest is history. Amy, now 81, is concerned with the future viability of her restaurant because of the of the minimum wage hike imposed by the city of Seattle, which far exceeds the federal minimum-wage rate of $7.25.

In June 2014, the city of Seattle adopted a new minimum wage of $15 per hour, highest in the nation and eclipsing the state minimum wage of $9.47 per hour (City of Seattle Legislative Records, 2014). The wage hike, which went into effect on April 1, 2015, phases in based on the schedule denoted in Table 1. After 2019, annual minimum-wage increases are tied to cost-of-living charges.

The idea of a $15 minimum wage first garnered attention in 2012 when fast-food workers from McDonald's, Burger King, Wendy's, Domino's, Papa John's, Kentucky Fried Chicken and Pizza Hut walked off their jobs in New York City, New York in strike for higher wages and better working conditions. This effort, orchestrated by New York Communities for Change, Service Employees International Union, UnitedNY, and the Black Institute, sparked a broad national movement and debate that has nudged various cities and states to raise the minimum wage. However, there are lobbyists, such at the National Restaurant Association, and politicians quashing efforts to enact minimum wage ordinances or municipal regulations. They feel it will stifle job opportunities for minimum-wage workers. One governor is threatening to cut state-shared revenues in cities that hike the state minimum wage on their own. Harry Holzer (2015), a public policy professor at Georgetown University, argues that a $15 wage hike will incentivize employers with low-skill workers to learn how to economize on their labor costs. He suggests that replacing servers with robots could become a viable option at some restaurants.

Minimum Wage Financial Impact

Amy called a meeting with her assistant manager, head chef, and bookkeeper. "I'm not sure how to cope with these wage bumps, the first one starting next month," stated Amy. "It is like an April Fool's joke!" I wish it was," stated Jerry Lopez, her longtime bookkeeper. "Twenty-nine states, plus the District of Columbia, have set their minimum wage above the federal level of $7.25 per hour. Now there is a push to increase the federal minimum-wage rate above $10.00. According to the National Restaurant Association, mandatory wage increases place a significant financial burden on restaurant owners who are also dealing with the

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Table 1

Schedule for 500 or Fewer Employees

Date	Wage Rate	Wage Increase % (base $9.47)
By April 2015	$11.00	16.16%
By January 2016	$12.00	26.72%
By January 2017	$13.00	37.28%
By January 2018	$14.00	47.84%
By January 2019	$15.00	58.39%

additional costs and regulatory complexity associated with the Affordable Care Act (National Restaurant Association, 2015). Furthermore, remember that the state of Washington prohibits the use of the federal tip credit, currently $5.12 per hour. So instead of paying tipped servers $2.13 per hour, we must pay the full minimum wage, even though our servers on average make about $16.00 to $18.00 per hour" (http://www.dol.gov/whd/regs/compliance/whdfs15.htm).

"I'm struggling with the fact that we must give the biggest pay raises to our servers who already make a decent wage," stated Amy with a chagrined look on our face. "Our survival will require increased menu prices and/or the cutting back of employee hours," replied the head chef, Mary Watson. "I know," agreed the assistant manager, Bill Wertz. "In a Seattle blog, Jeremy Hardy, the owner of 15th Ave's Coastal Kitchen, stated that the initial rise in the minimum-wage rate is forcing him to increase menu prices four percent and re-engineer front and back of the house schedules. However, he feels that a potent elixir of adjustments would be necessary as the ramp-up to $15 moves ahead" (Cohen, 2015).

"Our current profit margin is around six percent," stated Amy. "The current labor cost is about 33 percent. If we do nothing in 2015, the labor cost could reach 38 percent with an $11.00 minimum-wage rate, wiping out profitability. Anthony Anton, President and CEO of the Washington Restaurant Association, predicts that the $15 minimum-wage rate will result in an average labor cost of 47 percent if owners of full-service restaurants in Seattle make no changes (Jones, 2015). I think we all understand that if labor costs are not carefully established and monitored in relationship to revenue, they will increase until profit is eliminated and losses are sustained (Dittmner and Keffee III, 2009). We need to take action now if Amy's Café is going to survive the minimum wage hike."

"A higher minimum wage represents a particular challenge for restaurants, which depend heavily on hourly workers," stated Jerry. "I just read a research report that maintains that restaurant operators will have a tough time passing higher labor costs on to customers. The report predicts that increasing menu prices will be difficult due to soft consumer spending and the high level of promotions and discounts throughout the industry (Moody's Investor Service, 2015).The minimum-wage hike could also harm Seattle's thriving hotel, tourism, and convention business. Seattle plans to double the size of its convention center by 2020. Hotel development is flourishing to meet current demand and in anticipation of the convention center's expansion."

"I just wonder if Seattle restaurants will prosper if they pay a minimum wage that is more than 50 percent higher than one faced by competitors in nearby suburbs," contemplated Mary. "Food sales may decline for Seattle restaurants when competitors located just outside of city limits are charging lower prices (Burtless, 2014). On the other hand, Seattle could win the competition for employees with higher wages."

Effects of Raising the Minimum Wage on Workers

A server, Hank Thomas, brought coffee to the meeting. "I have overheard your conversations about the minimum-wage hike," stated Hank. "What are your thoughts on the subject?" asked Amy. "I think the minimum-wage hike is long overdue," quickly responded Hank. "While this may be viewed as a politically motivated mandate, it can be turned into an advantage. For example, smoke-free legislation has resulted in cleaner restaurants environments, a proven drawing card for diners. So many restaurant workers throughout this country do not earn enough in wages or work hours to survive. Significantly boost their wage rates and you will probably get one of the most loyal and productive workforces as well as the lowest employee theft figures in the industry." "Hank, that is a good point," replied Amy. "A common assumption is that labor rates equal labor costs (Cascio, 2006). Our retention rate could be higher but pay, in my opinion, is just one contributing factor."

"Amy, how are we going handle the implementation of the minimum-wage rate," inquired Jerry. "For example, Henry's current wage rate is $11.00 per hour. He is a dependable line cook that has worked at Amy's Café for three years. If we raise a new employee's wage rate from $9.47 per hour to $11.00, will Henry expect a pay increase that reflects his experience?" "Yes, we need to assess the effect of the minimum-wage rate increase on our compensation structure," replied Amy. "Our employees must be compensated fairly for their contributions. What employees perceive as fair and not fair can affect their motivation, attitudes, and behaviors" (Adams, 1963).

Action Plan

Amy thought about what actions could be taken to minimize the impact of the minimum-wage hike. "This situation is much more complex than it appeared at first," uttered Amy. "We must avoid actions that at best only temporarily alleviate the problem or, at worst, may even trigger other problems. A framework or criteria (see Table 2) for evaluating possible actions is needed" (Lundberg and Young, 2009).

Amy, let's develop an action plan," stated Jerry with a sense of

Table 2

Action-Selection Criteria

Criteria	Action Assessment Questions and Factors to Consider
Strategic Fit	Is the action consistent with the mission and values of Amy's Café? Will it be acceptable to employees and/or customers?
Ethicality	Is the action legally and ethically appropriate for Amy's Café? Is it understood as the right thing to do from an organizational, community, cultural, and societal perspective?
Pragmatic Feasibility	Is the action cost-effective? Is there enough expertise and resources available to support the action? Will it contribute to the longer-run well-being of the business and its employees?
Implementation Timing	Should the action be taken immediately? Or, can it be delayed somewhat? Or, is it best enacted over a period of time?

urgency. "We cannot afford to do nothing!" "I know Jerry," replied Amy somberly. "I know of at least one restaurant that is shutting down. "The owner feels that it is hard to make a business plan work if you have to pay $15 per hour. She decided to exercise an escape clause in her 10-year lease, rather than lock in for another five years with her house as collateral" (Wang, 2015).

"Amy, we will survive the minimum-wage hike?" inquired Mary. "We are a resilient business," replied Amy with a determined nod. "Resiliency is derived from the Latin word resilire, meaning to leap back. Amy's Café has weathered many storms, always bouncing back stronger with new strengths and abilities. When we stare down reality, we prepare ourselves to act in ways that enable us to survive hardships (Coutu, 2002). We need to involve all the employees in identifying possible actions."

Jerry quickly added, "And we need to share the monthly profit and loss (P&L) statement with employees for them to understand the gravity of the situation. This approach worked well for one restaurant owner whose employees were unaware of his restaurant's financial woes. After sharing the P&L and explaining what each line item meant, he noticed positive attitudinal and behavioral changes in his employees. In the kitchen, employees were more diligent in portioning and handling products, and servers were more attentive to their customers than before. Consequently, profit margins improved. Transparency is the key to gaining employee trust and engaging them in the task at hand" (O'Toole and Bennis, 2009).

Amy sighed as she stood up and looked at Jerry and Mary with a steady gaze and thought carefully. "We're an old fashioned business. Our building is in good shape but we have old kitchen and point-of-sale (POS) equipment. The menu has grown more complex and sophisticated over the years. The manual labor scheduling is a bit cumbersome too. This and other processes could be streamlined to gain cost and operational efficiencies."

One more thing to consider is a no-tipping policy," stated Jerry. "I know that replacing the age-old tipping system is controversial but it may be a way to increase menu prices to cover higher wages. Ivar's Salmon House hiked the minimum-wage rate to $15.00 and removed tipping, raised their prices 21 percent, and allocated 8 percent of the sales as the tip pool, which is distributed to all back and front of the house employees based on hours worked. Guests are paying about four percent more for a meal (Ivar's Inc., 2015). Rather than raising menu prices, other restaurant owners are eliminating tips but adding a service charge. The rules governing service charges are confusing though. Both state law and Seattle's minimum-wage ordinance require restaurants to disclose on menus or receipts what percentage of a service charge goes to employees, even though it is not technically required for them to receive anything (Garbes, 2015). The Whales Inn has the following disclosure on its menu: 'A 20 percent service charge will be added to each check. One-hundred percent of this charge is paid to employees. Sixty-two and one-half percent of this charge is paid to employees directly serving the customer.'" "Interesting and perplexing information," replied Amy.

"The value that we offer to customers resonates with them, as reflected in the popularity of Amy's café. However, the rise in minimum wage will require us to adjust our business model or way of doing business to deliver the same dining experience. Key business-model components that need addressing are the (Johnson, Christensen, and Kagermann, 1996):

- **Profit Formula:** The blueprint that defines how Amy's Café creates value for itself while still providing the same value to its loyal patrons through factors such as pricing, cost structure, and margin.
- **Resources**: The assets required to deliver the value proposition to targeted customers, which includes employees, technology, products, facilities, and equipment
- **Processes**: How value will be delivered to both customers and Amy's Café by using processes, such as scheduling, training, service, and prep to leverage resources."

Discussion Questions

1. In your opinion, what are the general pros and cons of raising the minimum wage?
2. How should Amy's Café restructure the pay scale to accommodate the minimum-wage rate hikes?
3. What actions (e.g., profit formula, resources, and processes) would you recommend to mitigate the minimum wage increase to ensure the long-term viability of Amy's Café? Use the framework in Table 2 for evaluating action options.

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