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**Do US Firms Have an Incentive to Comply
with the FLSA and the NLRA?**

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21-9 Do US Firms Have an Incentive to Comply with the FLSA and the NLRA?

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ABSTRACT

To what extent do US firms have an incentive to comply with the Fair Labor Standards Act (FLSA) and the National Labor Relations Act (NLRA)? I examine this question through a simple comparison of the expected costs of noncompliance (in terms of legal sanctions) to the profits firms can earn through noncompliance. In the case of the FLSA minimum wage and overtime provisions, typical willful violators are required to pay back wages owed and in some cases additional penalties, if detected by the Department of Labor (DOL). Based on available data on the penalties levied, a typical firm would need to expect a chance of at least 78–88 percent that its violation would be detected in order to have an incentive to comply with the FLSA. In practice, the probability of detection many firms can expect to face is likely much lower than this. In the case of the NLRA, a firm that fires a worker illegally is required to reinstate the worker with back pay if the violation is detected. Based on empirical estimates of the effect of unionization on firm profits, a typical firm may have an incentive to fire a worker illegally for union activities if this illegal firing would reduce the likelihood of unionization at the firm by as little as 0.15–2 percent. These analyses illustrate that neither the FLSA nor the NLRA penalty and enforcement regimes create sufficient incentive to comply for many firms. In this context, the substantial evidence of minimum wage and overtime violations, and of illegal employer behavior toward unions, is not surprising.

JEL codes: J38, J58, K31

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EXECUTIVE SUMMARY

The Fair Labor Standards Act (FLSA) and the National Labor Relations Act (NLRA) are two bedrocks of US worker protection. The FLSA enshrines workers' rights to earn the minimum wage and overtime pay. The NLRA grants workers the right to organize and collectively bargain with their employer. But for worker protection laws to be effective, there must be incentives for firms to comply. What gives a firm a hard economic incentive to comply with these laws? A purely profit-maximizing firm makes a simple calculus: comply if the expected costs of noncompliance outweigh the profits that can be made through noncompliance.

This working paper argues that the federal penalty regime for FLSA and NLRA violations creates very little financial incentive for many companies to comply. The penalties companies can expect to pay if they are caught violating the federal minimum wage or overtime pay rules, dismissing workers for union organizing, or failing to bargain in good faith with a union are often relatively small compared to the profits that can be earned through noncompliance—particularly when weighed against a small probability of detection of the violation for many firms.

Why is this the case for the FLSA? While minimum wage and overtime violations can in theory incur large penalties under the FLSA, in practice most firms pay relatively little. Detected violators of federal minimum wage and overtime laws must pay back wages to workers who were underpaid. Violators may also be required to pay up to an equal amount in liquidated damages, but while this often occurs in court actions, the evidence indicates that it occurs in only a minority of investigations by the Department of Labor (DOL). The DOL may also require willful and/or repeat violators to pay civil monetary penalties in addition to back wages and liquidated damages, but only 11 percent of detected FLSA violations are considered repeat and/or willful, nearly half of these are not required to pay any civil monetary penalty, and, even when levied, typical penalties are relatively small (with only 13% of repeat and/or willful violators required to pay a penalty of more than \$1 per dollar of back wages owed). Finally, while the FLSA provides for criminal prosecution in the case of serious violations, it is extremely rare: there were 10 criminal convictions for violation of the FLSA's minimum wage or overtime provisions during 2005–16 (a period during which the DOL identified nearly 3,000 willful violations).

What does this mean for compliance incentives? A firm's incentive to comply with the FLSA depends on the probability of detection and on the penalty it expects to pay if found non-compliant. But since most violating firms pay relatively small penalties, the FLSA enforcement system can only create a meaningful deterrent if the probability of detection firms expect is very high.

Specifically, we can calculate a rough threshold probability firms need to expect to give them an incentive to comply under different penalty scenarios. These calculations suggest that a firm which expects to face the typical penalty levied on first-time violators by the DOL would have to expect at least an 88 percent probability of detection to have an incentive to comply. If the firm also expects liquidated damages to be levied, it would have to expect a 47 percent probability of detection to have an incentive to comply. Even for the most egregious first-time violators, which might expect to have to pay liquidated damages *and* a very high civil monetary penalty, the expected probability of

detection must be at least one in three to create an incentive to comply with the law. Higher penalties are levied on repeat violators, but even then, the typical repeat violator detected by the DOL would have to expect a probability of detection of more than 78 percent to have an incentive to comply (or 44 percent if liquidated damages are expected to be levied). For many if not most firms, the actual probability of detection is likely substantially lower than this. Limited resources for federal investigation and inspection mean that for some firms, the probability of a DOL inspection in any given year may be as low as 2 percent even in sectors with a high risk of noncompliance. And while for some firms the threat of a worker complaint leading to either a DOL investigation or a collective action lawsuit will be enough to incentivize compliance, in many cases worker complaints are unlikely: workers may be unaware that their pay represents a violation of minimum wage or overtime requirements, unable to spare the time or resources to file a complaint or bring a suit, or unwilling to complain because of fear of retaliation, involvement with the legal system, or job loss. This is particularly likely to be true for the most vulnerable workers.

What about the NLRA? The situation is even starker for workers' rights to organize and bargain collectively. The NLRA only allows “make-whole” remedies, which compensate workers for their direct losses arising from a violation, with no possibility of meaningful financial penalties. For example, if a firm dismisses a worker for her union activities, the National Labor Relations Board (NLRB) may require the firm to reinstate the worker and pay her back wages for lost employment income, but no further penalties may be levied. The potential benefit to a firm from averting unionization, in contrast, can be very large: David Lee and Alexandre Mas (2012) estimate that unionization on average reduces firms' equity value by 10 percent, or around \$60,000 per unionized worker. Using this estimate, calculations in this paper suggest that a typical profit-maximizing firm, comparing the potential cost of paying back wages to the potential benefit of averting unionization, would have a compelling financial incentive to dismiss a worker for union activities—even if the firm knew *with certainty* that it would be caught and penalized by the NLRB—if this dismissal would reduce the likelihood of unionization at the firm by less than 2 percent, and perhaps by as little as 0.15 percent.

Overall, this analysis finds that there is very little purely financial incentive for firms to comply with federal minimum wage or overtime laws, or with union organizing protections. Instead, for many firms the enforcement of these core federal workplace protections appears to rely largely on goodwill or reputational concerns. In this context, the substantial evidence of minimum wage and overtime violations (wage theft) and of illegal employer behavior toward unions should be no surprise. The lack of a meaningful federal deterrent for many firms leaves workers at unethical companies insufficiently protected from abuse, and creates an unfair competitive environment for companies that obey the law.

How can deterrence be increased? Increased resources for enforcement agencies are important in order to increase the likelihood of violations being detected. But, while increasing enforcement resources is necessary, the analysis in this paper suggests this alone may not be sufficient. For the FLSA, even with substantially more resources for federal wage and hour inspections, it may not be possible to generate sufficiently high probabilities of detection to generate meaningful compliance incentives under the existing penalty structure. And

for the NLRA, even when facing certain detection of illegal behavior, penalties are so small that many firms likely still have a substantial incentive to break the law. **To ensure that all companies have an incentive to comply with the law, substantially higher penalties for minimum wage and overtime violations and for violations of union protections are necessary.**

1. QUANTIFYING INCENTIVES TO COMPLY: A COST-BENEFIT FRAMEWORK

How can one quantify a firm's incentive to comply with the law? A long tradition in economics applies a cost-benefit framework to decisions to comply with the law.¹ Under this framework, a profit-maximizing company will comply with a law if the expected costs of non-compliance, if a violation is detected, exceed the expected extra profits the company can make if it does not comply:

$$\text{probability of detection} \times \text{expected cost if detected} > \text{profits from noncompliance}$$

In this paper, I focus on the federal legal penalties for violations of the FLSA and the NLRA. Using the provisions in the legal statutes, empirical evidence on penalties levied, and estimates of the profits firms save from noncompliance with minimum wage, overtime, or labor law protections, I estimate the degree to which firms have a *purely financial* incentive to comply with federal minimum wage, overtime, and labor law.

This approach assumes that at least some firms actively decide whether or not to comply.² This is not an unreasonable assumption. While some employers violate the FLSA or NLRA inadvertently, the evidence is clear that a nontrivial number of employers intentionally violate minimum wage, overtime, and union protections,³ and that higher penalties deter at least some violations.⁴ Finally, it is often not possible to draw a bright conceptual line between inadvertent and intentional underpayment. Firms' incentive to *learn about* labor and employment protections and ensure that they and their managers comply with them is greater, the greater the penalty firms expect to face if their violations are detected.

In this analysis, I do not consider reputational or ethical costs of noncompliance. While these do matter for many firms' compliance decisions (Ji and Weil 2015, Johnson 2020) it is insufficient for a law to rely *only* on reputation or ethics: if so, workers at unscrupulous companies suffer, and ethical companies are at a competitive disadvantage.

1 Becker (1968) is widely credited with having begun this tradition. Ashenfelter and Smith (1979), Grenier (1982), Chang and Ehrlich (1985), Lott and Roberts (1995), Weil (2008, 2010), Kleiner and Weil (2012), Hallett (2018), and others apply the cost-benefit framework to various labor and employment law violations.

2 My work is in the "deterrence-based" tradition, rather than the "compliance-based" tradition (which assumes that noncompliance is mostly inadvertent). See, e.g., Judy Fudge's work, outlined in Metcalf (2018).

3 Bernhardt et al. (2013) present evidence that "noncompliance with employment and labor laws is becoming a key feature of employers' competitive strategy at the bottom of the U.S. labor market." Mattera (2018), in an analysis of 1,200 collective action cases and 4,200 federal and state wage theft actions, suggests that wage theft is part of the "business model" for many large corporations. Rhinehart, Windham, and Mishel (2020) present evidence that some firms strategically violate labor law to avoid unionization.

4 Galvin (2016) and Clemens and Strain (2020) show that the prevalence of minimum wage underpayment is substantially lower when state-level penalties are higher.

I focus on the federal level in this paper. While state-level protections and enforcement are also vital, incentives to comply at the federal level are important to ensure both that workers throughout the country are protected regardless of the state in which they work and that companies are not incentivized to shift production locations to avoid having to comply with the law in a race-to-the-bottom dynamic.

2. MINIMUM WAGE AND OVERTIME PAY: THE FAIR LABOR STANDARDS ACT

Under the FLSA, it is illegal to pay covered, nonexempt workers less than the federal minimum wage (\$7.25 an hour). Similarly, FLSA overtime rules require that covered workers be paid at least one-and-a-half times their regular pay for any time worked in excess of 40 hours per week.⁵

Penalties and Enforcement

Any employer found to have violated the FLSA minimum wage or overtime rules must pay affected employees back wages (to make up the difference between what the employees were actually paid and what they should have been paid) covering a period of up to two years.⁶ In addition, a violating employer may be subject to further costs:

- Liquidated damages: The employer may be required to pay affected employees liquidated damages of up to the amount of the back wages owed (unless the employer can show that the violation was in good faith).⁷
- Civil monetary penalty: The DOL may require repeat or willful violators to pay a civil monetary penalty of up to \$2,014 for each violation.⁸
- Hot goods embargo: The DOL may use “hot goods” authority to embargo goods which have been manufactured in violation of the FLSA.
- Criminal prosecution: The DOL may refer willful violators for criminal prosecution, which can lead to a fine of up to \$10,000, and—if a repeat violator—possible imprisonment for up to six months.

There are two primary mechanisms to enforce the FLSA: (1) a Department of Labor (“DOL”) investigation, triggered either by an employee complaint or a targeted enforcement action, or (2) a court action brought by affected

5 Professional, executive, and administrative employees and some other groups are exempt from the FLSA. Workers are also covered only if their employer is large enough (gross sales greater than \$500,000) and/or engaged in interstate commerce.

6 Specifically: the statute of limitations is two years, except for willful violations (three years) or criminal prosecutions (five years).

7 Specifically, the 1947 Portal-to-Portal Act (29 U.S. Code section 260) sets out a good faith defense to liquidated damages if “the employer shows... that the act or omission giving rise to such action was in good faith and that he had reasonable grounds for believing that his act or omission was not a violation” of the FLSA.

8 A violation can be defined per person based on the number of employees an employer paid unlawfully, per week of wages owed. The FLSA stipulates that the size of the business and gravity of the violation should be considered when determining the size of the penalty.

employees, either individually or as part of a collective action (which can cover all employees “similarly situated” as long as they provide written consent to opt in to the proceedings).

This penalty structure suggests that the maximum cost an employer may incur if it violates the FLSA can be large. In practice, however, the actual penalties most firms pay are relatively small. Liquidated damages, while the norm in court actions, are rarely levied in DOL investigations. Only a small minority of violations are deemed willful by the DOL, and civil monetary penalties for willful and/or repeat violators are usually small (and often zero). The DOL’s hot goods authority in practice is restricted to a few industries. And criminal convictions are extremely rare. I discuss each of these in more detail below.

Liquidated damages appear to be assessed only in a minority of cases

In court actions against employers (brought collectively or individually by employees), liquidated damages are typically levied unless the employer can demonstrate that the violation was in good faith.

However, in DOL investigations, publicly available materials suggest that liquidated damages are rarely levied.⁹ For violations in the 1990s and 2000s, liquidated damages were almost never assessed by the Department of Labor (Weil 2018). For example, David Weil (2010) estimates that for cases concluded between 2003 to 2008, “less than one half of one percent of cases had liquidated damages computed by investigators and zero cases had liquidated damages assessed,” and Kim Bobo (2011, p. 1871) writes that “I had never heard of workers getting liquidated damages when they filed complaints with the Department of Labor.” In more recent years, particularly under Weil’s tenure at the DOL’s Wage and Hours Division, the DOL has increased its use of liquidated damages (Weil 2018). The extent to which this increase occurred is unclear from publicly available information.¹⁰

Few violations are deemed willful, meaning few are eligible for civil monetary penalties

The Department of Labor has the authority under the FLSA to levy civil monetary penalties on willful or repeat violators. However, the vast majority of minimum wage or overtime violations detected by the DOL were first-time (detected) violations and were not deemed to be willful. They were therefore not eligible for

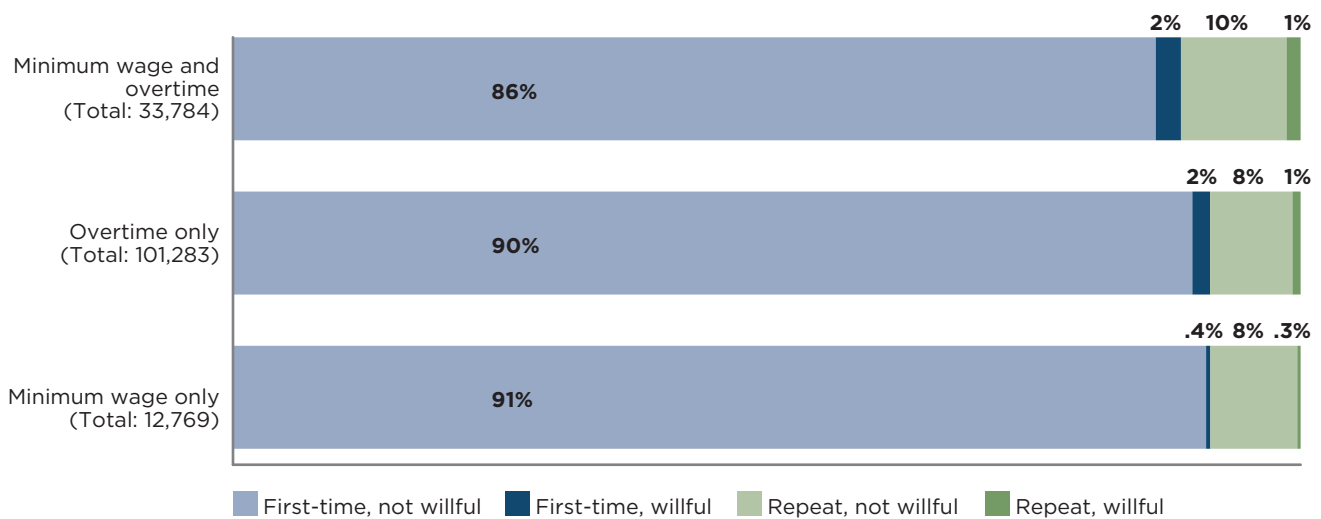
9 According to Section 53c00 of the DOL Wage and Hour Division’s *Field Operations Handbook*, the DOL’s decision to pursue liquidated damages is related to the employer’s ability to demonstrate good faith in its violation of the FLSA: the employer must demonstrate both (1) a subjective belief that it was acting in good faith and (2) that its actions were objectively reasonable. Excerpts from the handbook are available at the website governmentattic.org and were obtained by this website through a FOIA request submitted in July 2017 (tracking number 836790).

10 The Department of Labor’s publicly available Wage and Hour Investigative Support and Reporting Database (WHISARD), which documents all wage and hour investigations, does not indicate whether liquidated damages were assessed in individual cases.

civil monetary penalties.¹¹ To be more precise: of the 148,043 cases since 2005 in which the DOL detected minimum wage or overtime violations with back wages owed, 91 percent were first-time violations.¹² Of these, 2 percent were found to be willful, and 9 percent of the repeat violations were found to be willful. This breakdown is similar whether the cases involved minimum wage underpayment, overtime underpayment, or both, as shown in figure 1.¹³

Figure 1

Share of FLSA violations deemed repeat and/or willful, among concluded DOL Wage and Hour Division actions, FY2005–20



Note: Rows do not always add to 100% due to rounding.

Source: Department of Labor WHISARD.

- 11 Determination of whether a firm is a “willful” violator has an element of subjectivity and historically the term has been defined relatively narrowly. The Supreme Court decision *McLaughlin v. Richland Shoe Co.* (1988) took “willful” to mean that “the employer either knew or showed reckless disregard for the matter of whether its conduct was prohibited by the statute.” The court’s definition excluded a violation based on “nothing more than negligence, or, perhaps, on a completely good-faith but incorrect assumption.” The DOL updated its guidance in 2016 to consider as willful cases where the party “knew that its conduct was prohibited by any of the Labor Laws or showed reckless disregard for, or acted with plain indifference to, whether its conduct was prohibited by one or more requirements of the Labor Laws.”
- 12 These data are from WHISARD (available at enforcedata.dol.gov), which contains data on “all concluded Wage and Hour Division actions since FY 2005.” The data in this paper were downloaded in March 2021 and last updated by the DOL on January 27, 2021. In this paper, I analyze the 148,043 cases in WHISARD which feature at least one violation of FLSA minimum wage or overtime provisions where back wages were found to be owed (i.e. excluding recordkeeping or notice-posting violations), in the 50 states and Washington, DC. For each case, the data include the back wages the employer agreed to pay for minimum wage and overtime violations, the number of employees due back wages, and the civil monetary penalties assessed under the FLSA. The database also flags whether an employer was found to be a repeat and/or willful violator. Unfortunately, it does not include information on liquidated damages.
- 13 Figure shows information for 147,836 of the 148,043 cases in the DOL WHISARD for which there is a positive amount of FLSA back wages owed. The discrepancy arises from 207 cases which are listed as having positive FLSA back wages but zero under each of the violation categories “minimum wage” and “overtime.”

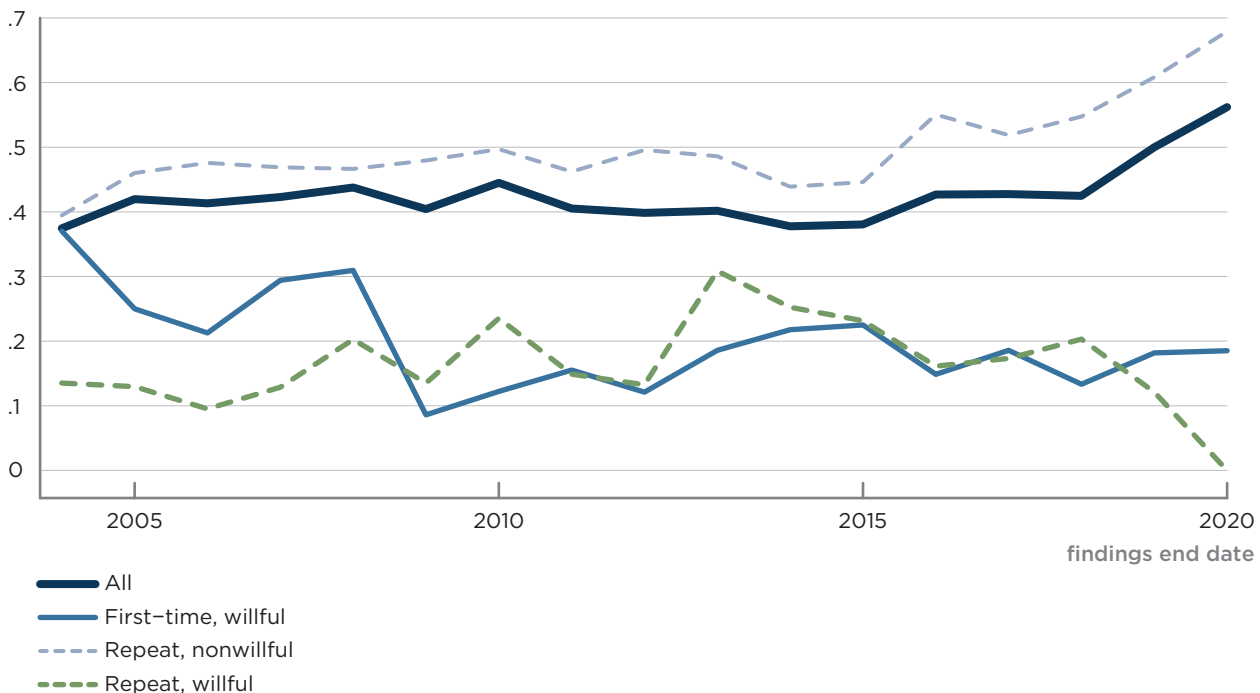
Nearly half of repeat and/or willful violations are not levied any civil monetary penalty

For repeat or willful violations the DOL can levy civil monetary penalties of up to \$2,014 per violation. A violation can be defined per employee, per week of wages owed, meaning that the maximum possible civil monetary penalty could in theory be quite large for many minimum wage or overtime cases. Yet in 41 percent of all repeat and/or willful cases since 2005, firms were required to pay no civil monetary penalty at all for their minimum wage or overtime violations¹⁴; instead, the maximum total penalty they might have faced is back wages plus an equal amount in liquidated damages. This pattern has remained roughly stable over time, and if anything recent years have seen an uptick in the share of violators *not* paying any civil monetary penalty (figure 2).

Figure 2

Share of repeat and/or willful FLSA minimum wage and overtime violations that were not assessed any civil monetary penalty, among concluded DOL Wage and Hour Division actions, FY2005–20

share of repeat/willful violations with no civil monetary penalty



Note: "Findings end date" refers to the latest date in which the Department of Labor (DOL) found violations.

Source: Department of Labor WHISARD.

¹⁴ Similarly, Weil (2010) showed that a civil monetary penalty was assessed in fewer than half of repeat FLSA violations identified by the DOL over 1998 to 2009.

In the cases where a civil monetary penalty is assessed, the amounts are often quite small

Table 1 illustrates the distribution of civil monetary penalties per dollar of back wages (which corresponds roughly to the penalty per dollar of wages the firm initially saved by violating the FLSA). The median first-time, willful violator was required only to pay a penalty worth 14 cents for each dollar of wages owed to its employees. The median repeat, nonwillful offender was required to pay a penalty of just 3 cents for each dollar of wages owed. Even for the most egregious violators—repeat *and* willful—the median offender had to pay a penalty of only 29 cents per dollar of wages owed, and only 21 percent of repeat and willful violators had to pay a penalty worth more than \$1 per dollar of wages owed. Nonetheless there have been some very high penalties: 1 percent of repeat, willful violators paid a civil monetary penalty worth more than \$10.45 per dollar of back wages owed.¹⁵

Table 1
Civil monetary penalties (CMP) assessed, per dollar of back wages, among DOL Wage and Hour Division actions, FY2005–20

Category	Cases	Share with zero CMP	CMP per dollar of back wages owed, percentiles and mean									
			P1	P5	P10	P25	P50	P75	P90	P95	P99	Mean
First-time, willful	2,504	18%	0	0	0	0.05	0.14	0.34	0.75	1.25	3.66	0.36
Repeat, nonwillful	12,242	48%	0	0	0	0	0.03	0.43	1.31	2.30	6.04	0.49
Repeat, willful	1,248	19%	0	0	0	0.09	0.29	0.82	2.10	3.86	10.45	0.91

Source: Department of Labor (DOL) WHISARD.

Overall, of the 148,043 FLSA minimum wage and overtime cases since 2005 where the DOL found that back wages were owed, *any* civil monetary penalty was levied in only 6.3 percent of cases, and a penalty of more than \$1 per dollar of wages saved was levied in only 1.4 percent of cases.¹⁶ These figures are likely overestimates of actual civil monetary penalties paid. Weil (2010) finds that firms often pay substantially lower civil monetary penalties than the value initially

¹⁵ Several sections of the DOL WHD *Field Operations Handbook*, Chapter 52, appear to discuss the criteria for assessing civil monetary penalties and deciding on their magnitude. Unfortunately, these sections are mostly redacted in the chapters made available to the public via a FOIA request in 2017 (see footnote 9). Section 52f15 of the handbook states that “CMPs [civil money penalties] must not be assessed in an amount related to the amount of back wages. We do not want to leave an impression that CMPs are anything like liquidated damages.” This suggests that the criteria for levying CMPs are not related to the severity of the offense in terms of the amount of wages unpaid.

¹⁶ Since repeat and/or willful cases make up 10.8 percent of all cases, this implies that any civil monetary penalty was levied in 59 percent of repeat and/or willful cases and a penalty of more than \$1 per dollar of wages saved was levied in 13 percent of repeat and/or willful cases. Note that recent years have seen a small increase in average penalties, particularly for repeat willful violators (appendix figures A1 and A2).

assessed by the DOL Wage and Hour Division (WHD): over 1998–2008 the civil monetary penalties ultimately deemed receivable were only 61 percent of the initial amount assessed on average.

Hot goods authority provides a substantial deterrent, but is limited to certain industries

The final element in the DOL's enforcement toolkit is the "hot goods" provision (FLSA section 15(a)), which allows the WHD to embargo goods manufactured in violation of the act. This creates a greater incentive for compliance in certain industries, both because it increases the probability of detection by incentivizing companies higher in the supply chain to monitor their subcontractors to avoid production delays and because it increases the cost of detection as the costs of the embargo can be many multiples of DOL fines (Weil 2005). Prior to the Obama administration, the hot goods provision was primarily used in the garment industry. According to Weil (2018), during his tenure as WHD administrator (2014–16), the DOL substantially increased its use of this provision in the garment industry and also used it in agriculture. For businesses in these industries, the increased use of the "hot goods" provision means that the expected cost of violations is likely to be larger—perhaps much larger—than other penalties. It is not clear to what extent the DOL uses the hot goods authority beyond garments and agriculture (Koltookian 2014, Weil 2010).¹⁷

Criminal convictions almost never occur

The FLSA enables criminal prosecution of willful violators, but only 10 convictions occurred for FLSA minimum wage or overtime violations over a recent 11-year period (2005–16; table 2).¹⁸ Relative to the total number of violations, this is so small as to be trivial: over the same period, the Department of Labor assessed roughly 113,000 FLSA minimum wage and overtime violations where back wages were owed, of which roughly 2,900 were found to be willful and therefore possible candidates for a criminal penalty.¹⁹ This means that, even *conditional* on a minimum wage or overtime violation being both detected and deemed willful by the DOL, firms face less than a 0.4 percent chance of a criminal conviction under the FLSA.²⁰ (State-level prosecutions appear to be somewhat more frequent; National Employment Law Project 2013.)

17 The 2018 version of the DOL WHD *Field Operations Handbook* recommends that the following five factors be considered when determining whether a hot goods action is appropriate: (1) history of prior violations, (2) employers that have missed payroll or that have financial problems and may be unable to pay back wages, (3) concealment or falsification of records, (4) temporary or transient workers, and (5) systemic violations.

18 Data obtained through an email request to the Bureau of Justice Statistics (data for 2005–2016 was the most recent data available as of February 2021).

19 The WHISARD database contains 113,417 FLSA minimum wage violations where back wages were owed, of which 2,925 were willful, during 2005–2016. The correspondence to years of convictions is not exact: WHISARD lists cases according to the last year in which violations occurred, rather than the year in which the investigation was concluded.

20 According to the 2018 version of the DOL WHD *Field Operations Handbook*, "It is the WHD's policy to treat all inexcusable or willful violations of the FLSA...as criminal or potential blacklist" (Section 81b01). An investigation for criminal prosecution will not be accepted "unless the evidence is such that there is a reasonable probability that a conviction will be obtained." Violations are considered "excusable if the employer can establish that he or she relied upon or acted in good faith, and in conformity with information given to him or her by a [wage hour investigator], other responsible representative, or the Federal Government."

Table 2
Number of convictions for minimum wage or overtime violations under the Fair Labor Standards Act, 2005-16

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Minimum wage	0	0	0	0	0	0	0	0	1	3	0	0
Overtime	1	1	2	0	0	1	1	0	0	0	0	0

Notes: Table shows number of defendants convicted under U.S. Code Title 29 Chapter 8 section 206 (minimum wage) and U.S. Code Title 29 Chapter 8 section 207 (overtime) in fiscal years 2005-2016 inclusive.

Source: Bureau of Justice Statistics, obtained on request.

Calculating the Probability of Detection Required to Incentivize Compliance

With the data about the range of penalties firms face under different circumstances, we can think through the cost-benefit analysis firms might undertake when considering whether to comply with federal minimum wage or overtime law. As outlined on page 4, a profit-maximizing firm will have an incentive to comply only if the expected costs of noncompliance (calculated by multiplying the expected financial penalty by the probability of detection) are greater than the expected benefits (the firm's savings as a result of underpayment).²¹ As Yang-Ming Chang and Isaac Ehrlich (1985) showed,²² for wage and hours violations this condition simplifies to suggest that the firm should comply if:

$$\text{Probability of violation being detected} \times \text{Penalty per dollar of unpaid wages} > 1$$

Intuitively, this is because each dollar of underpayment translates roughly into an additional dollar of profit for the firm (the right-hand side of the expression), while the expected cost of each dollar of underpayment is the product of the probability of detection and the penalty per dollar of unpaid wages (the left-hand side). This means we can ask: **What is the minimum probability of detection required to incentivize compliance with FLSA minimum wage and overtime laws?** As equation (1) suggests, the minimum probability of detection required to incentivize compliance is simply the reciprocal of the expected penalty per dollar of unpaid wages:

$$\text{Minimum probability required to incentivize compliance} = \frac{1}{\text{expected penalty per dollar of unpaid wages}} \quad (1)$$

This formula will overestimate the benefit of non-compliance to the extent that efficiency wage effects are important: to the extent that paying higher

21 For a similar analysis with UK data, see Judge and Stansbury (2020).

22 Following Ashenfelter and Smith (1979). Weil (2005) used this framework to evaluate the incentives for firms to comply with minimum wage standards in apparel.

wages reduces (costly) turnover or increases employee productivity, paying a wage \$1 higher will lead to less than \$1 in foregone profit.²³

To estimate the minimum probability required to incentivize compliance, we need estimates of the expected penalty per dollar of back wages unpaid. I use the DOL data on actual penalties levied to evaluate this quantity separately for first-time and repeat violators (since the latter are eligible for a higher penalty) in four scenarios where a firm has underpaid \$1,000. Each scenario involves different combinations of liquidated damages and civil monetary penalties, as outlined in table 3.

Table 3

Different scenarios for analysis of the minimum expected probability of detection required to incentivize compliance

Scenario	Back wages?	Liquidated damages?	Likelihood of being deemed “willful”?	Civil monetary penalty?
1	Yes	No	Average likelihood	Median penalty
2	Yes	No	Certain	Median penalty
3	Yes	Yes	Certain	Median penalty
4	Yes	Yes	Certain	95th percentile

Note: Hypothetical scenarios by author.

Based on the publicly available data, the most likely scenario for a firm caught violating the FLSA by the DOL is either Scenario 1 or Scenario 2—the firm pays back wages, does not pay liquidated damages, and pays the median civil monetary penalty if its violation is deemed willful. Since liquidated damages are levied in only a minority of DOL cases, Scenario 3, involving liquidated damages *and* the median civil monetary penalty, is likely less common and so less salient for firms. Scenario 4, involving liquidated damages and the 95th percentile civil monetary penalty, should be seen as an extreme case, applying only to the most egregious violators.²⁴ For firms taken to court for FLSA wage and hour violations in an individual or collective action, the outcome is likely to be somewhere between Scenario 1 and Scenario 3, as back wages are always awarded and liquidated damages are often also awarded.

23 See, for example, Akerlof and Yellen (1986) for a discussion of efficiency wage theories. There is substantial evidence that turnover responds to pay: see, for example, Bassier, Dube, and Naidu (2019) and Manning (2021). Emanuel and Harrington (2021) also provide evidence of substantial effects of higher wages on productivity in the context of warehousing and call centers.

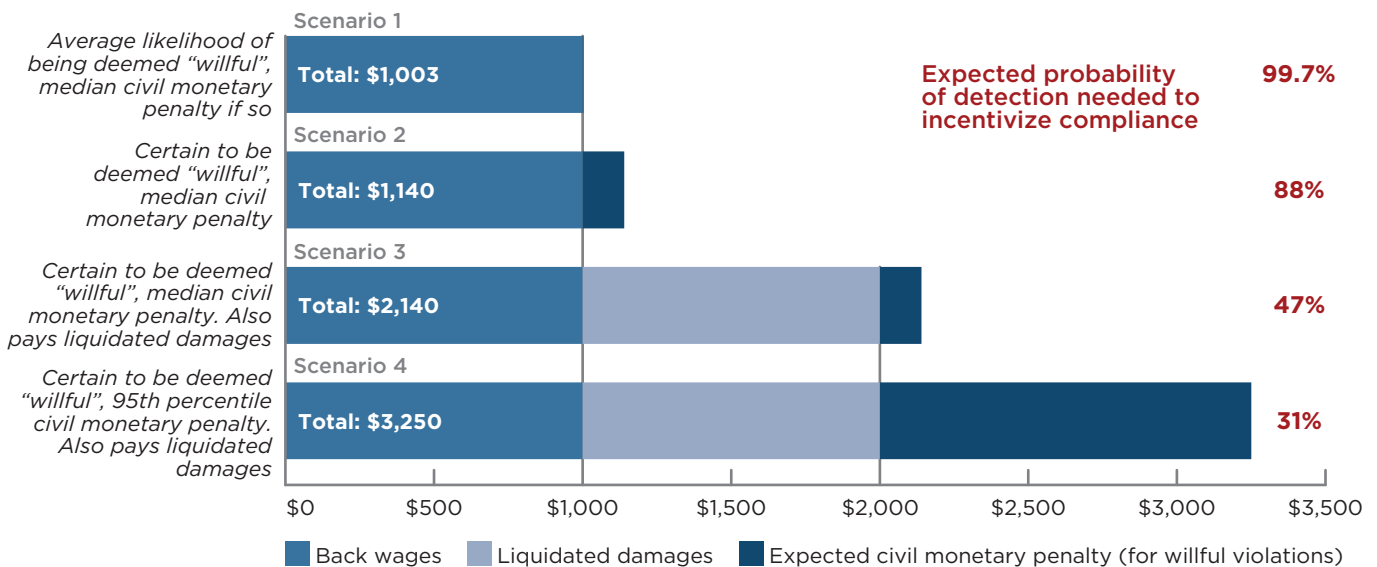
24 Given the rarity of criminal prosecutions, I do not consider this a likely outcome that firms expect. I also do not consider the “hot goods” provision, since it appears to be used only in the garment industry and agriculture.

Most first-time violators must expect near-certain detection to have an incentive to comply

Figure 3 illustrates expected penalties for a first-time violator of the FLSA in each of the four scenarios. It also shows the minimum probability of detection the firm must expect in order to have an incentive to comply with the FLSA (calculated per equation (1) as the reciprocal of the expected penalty).

Figure 3

First-time violators: Estimated cost of detection by the DOL if a firm has underpaid the minimum wage or overtime by \$1,000



Note: This figure shows the estimated cost to a firm of detection by the Department of Labor (DOL), if it has underpaid the minimum wage or overtime by \$1,000, and is a first-time violator. Each scenario includes the firm paying \$1,000 in back wages, and Scenarios 3 and 4 also include payment of liquidated damages. For each scenario, the expected civil monetary penalty is calculated based on different assumptions about the likelihood of the firm's actions being deemed willful. Likelihood of being deemed willful, and median civil monetary penalties if so, are estimated from WHISARD.

Source: Author's calculations; Department of Labor WHISARD.

Scenario 1 illustrates the scenario facing the typical first-time violator. In this scenario, we assume the firm expects to have to pay back wages, to face an average likelihood of being deemed "willful" (about 2 percent), and to pay the median penalty if so. This makes the total expected cost of a \$1,000 wage violation \$1,003 (\$1,000 in back wages plus \$3 in expected civil monetary penalties). Following the logic laid out in equation (1) above, this means that the firm would have to expect detection with a 99.7 percent probability to have an incentive to comply with the law.²⁵

²⁵ This is because the firm expects a 98 percent likelihood that it will not be found to have been a willful offender and so will only have to pay \$1,000, and expects a 2 percent likelihood that it will be found willful. If it is found willful, it expects the median civil monetary penalty paid by first-time willful offenders per dollar of back wages owed, which is \$0.14 according to DOL WHISARD (and therefore amounts to a penalty of \$140 for a violation worth \$1,000 in underpaid wages). As Weil (2010, p.49) notes, if most first-time violators simply have to pay back wages and no other penalties, "a rational employer who can attract a workforce paying below the minimum wage actually should violate since the cost of doing so (the first time) is simply the amount of back wages owed to workers (i.e., what a compliant employer should have been paying all along)."

Scenario 2 illustrates the scenario facing the typical first-time willful violator. In this scenario, we assume the firm expects its violation will be deemed willful *with certainty*, and it will be subject to the median civil monetary penalty for willful first-time violations as well as having to pay back wages: the expected total cost of a \$1,000 wage violation is therefore \$1,140 (\$1,000 in back wages and an expected \$140 in civil monetary penalties). A firm expecting to face a total cost of \$1,140 for its violation would have to expect detection with an 88 percent probability or more to have an incentive to comply with the law.

If liquidated damages are levied—which does not happen in the majority of DOL cases—the probability of detection firms must expect to have an incentive to comply with the law falls quite substantially. Specifically: Scenario 3 assumes that the firm expects to be deemed willful with certainty, to pay the median civil monetary penalty for willful first-time violators, *and* to have to pay liquidated damages. In this case, the total cost of a \$1,000 violation rises to \$2,140 (\$1,000 in back wages, \$1,000 in liquidated damages, and \$140 in civil monetary penalties), meaning that the firm would have to expect detection with a 47 percent probability to have an incentive to comply with the law.

Even for the most severe first-time violators, the probability of detection firms must expect to incentivize compliance is around one in three. Scenario 4 illustrates that, if a firm expects to pay a very high civil monetary penalty if caught—the 95th percentile penalty levied on first-time, willful violators—and to have to pay back wages *and* liquidated damages, the total expected cost of a \$1,000 wage or hour violation rises to \$3,250, implying that the firm would have to expect a probability of detection of at least one third to have an incentive to comply with the law.

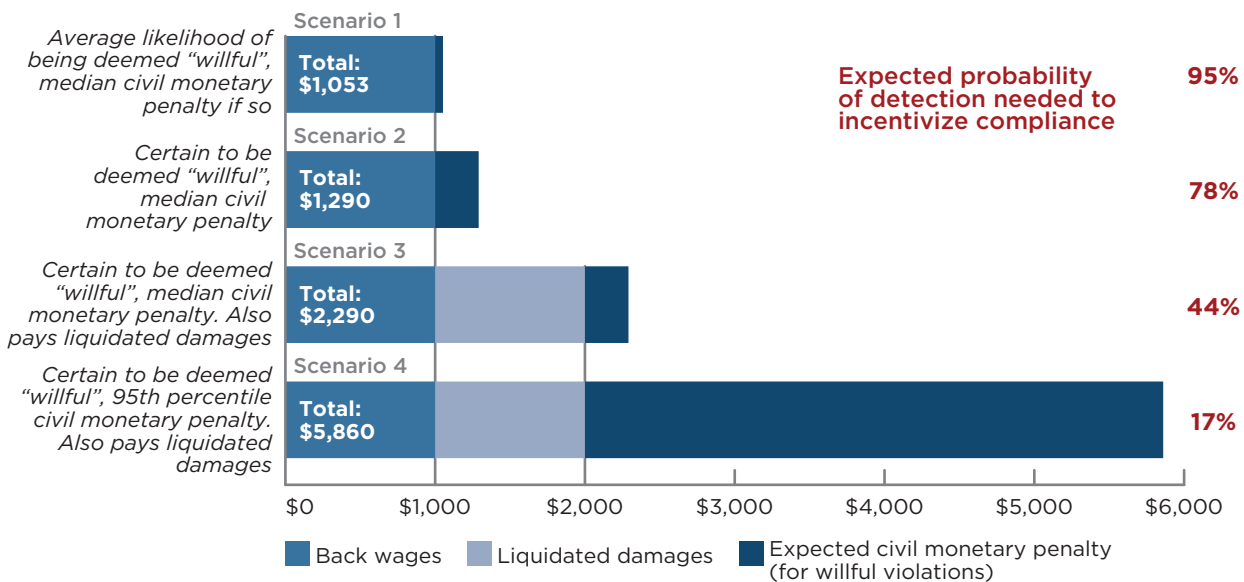
Repeat violators face higher penalties, but the average repeat violator must still expect to be detected with at least 78 percent probability to have an incentive to comply

Figure 4 repeats the above scenario analysis, but with a repeat violator—a firm that the DOL has previously found to have underpaid the minimum wage or overtime.

Scenarios 1 and 2 are the most likely scenarios for repeat violators. Scenario 1 assumes that a firm with a prior detected FLSA violation (i.e. a repeat violator) expects that it will have to pay back wages, that it has the average likelihood of being deemed willful (for a repeat violator), and that it will pay the median civil monetary penalty for repeat nonwillful violations if its violation is not deemed willful, and the median civil monetary penalty for repeat willful violations if its violation is deemed willful. This leads to an expected total cost of \$1,053, meaning that the expected probability of detection required to incentivize compliance would be 95 percent. In Scenario 2, the firm expects to have to pay back wages, expects to be deemed willful, and expects to have to pay the median civil monetary penalty for repeat willful violations, making the expected total cost of the violation \$1,290. In this case, the firm must expect a probability of detection of 78 percent or more to have an incentive to comply.

Figure 4

Repeat violators: Estimated cost to a firm of detection by the DOL if the firm has underpaid the minimum wage or overtime by \$1,000



Note: This figure shows the estimated cost to a firm of detection by the Department of Labor (DOL), if it has underpaid the minimum wage or overtime by \$1,000, and is a repeat violator. Each scenario includes the firm paying \$1,000 in back wages, and Scenarios 3 and 4 also include payment of liquidated damages. For each scenario, the expected civil monetary penalty is calculated based on different assumptions about the likelihood of the firm's actions being deemed willful. Likelihood of being deemed willful, and median civil monetary penalties for repeat nonwillful and repeat willful violations, are estimated from WHISARD.

Source: Author's calculations based on data from Department of Labor WHISARD.

In Scenario 3, the firm expects to have to pay liquidated damages alongside back wages and the median civil monetary penalty for repeat willful violators. The total expected cost of the violation becomes \$2,290, meaning the expected probability of detection required to incentivize compliance is 44 percent.

Finally, Scenario 4 considers an extreme case where the firm expects to have to pay a civil monetary penalty at the 95th percentile (\$3.86 per dollar of back wages) as well as liquidated damages and back wages. In this case, the firm would have to pay a substantial penalty of \$3,860 in addition to back wages of \$1,000 and liquidated damages of \$1,000, for a total expected cost of the violation of \$5,860—implying that the minimum probability of detection required to incentive compliance is relatively low at 17 percent.

Overall, this analysis suggests that for all but the most serious repeat and willful violators, detection rates would need to be extremely high for the current DOL penalty regime to be an effective deterrent.

In fact, this analysis may represent an *overestimate* of the costs firms face when they are found to have violated the minimum wage or overtime laws. This is because I assume that the variable "amount of back wages agreed to" in the DOL dataset reflects the actual back wages the firm failed to pay—but in practice, firms may pay less in back wages than the value of their initial underpayment. There are several reasons for this. First, there is a two-year statute of limitations for

nonwillful violations, and a three-year statute of limitations for willful violations, so for multiyear violations the back wages paid are often less than the full amount of income workers should have received. Second, firms may have kept bad records, which means that the DOL may not be able to prove the full amount that the firm owes workers (Bobo 2011). Third, employers often reach a settlement that requires them to pay back only a portion of the wages underpaid (Hallett 2018, Cooper and Kroeger 2017). Understanding whether firms' incentives to comply with the minimum wage are greater or less than our estimates here requires balancing these factors against the possibility of efficiency wage effects on productivity and turnover (as discussed earlier in this section). The presence of efficiency wage effects would cause us to overestimate the minimum probability of detection required to incentivize compliance (i.e. firms have a *greater* incentive to comply than we estimate), while the fact that our data likely overestimates the actual costs firms pay when found noncompliant would cause us to underestimate the minimum probability of detection required to incentivize compliance (i.e. firms have *less* incentive to comply than we estimate).

What Is the Probability of Detection That Firms Actually Face?

How do the required probabilities of detection estimated in the previous section compare to the actual probabilities of detection that firms face? It is by definition impossible to obtain good data on the probability of detection faced by firms that violate the minimum wage or overtime laws because it is impossible to estimate accurately the number of firms that are noncompliant. However, it is possible to get some idea of whether most firms' probability of detection is in the same order of magnitude as the ranges necessary for them to have an incentive to comply. I analyze this for each of the three main enforcement channels: a DOL-initiated investigation, a worker complaint to the DOL leading to an investigation, or a worker bringing individual or collective court action against the firm. I also briefly discuss state-level enforcement. Overall, the analysis in this section finds that the actual probabilities of detection many firms face are likely to be substantially lower than those necessary to generate meaningful compliance incentives.

Investigations by the DOL alone cannot generate a high enough probability of detection to give all firms an incentive to comply

The DOL WHD statutes cover an estimated 7.3 million establishments and 135 million workers (Weil 2018). Katie Hamaji and colleagues (2019) estimate that for each WHD investigator in 2018, there were 175,000 workers covered by the FLSA (compared to a ratio of 1:69,000 in 1978)—meaning the probability that any given establishment will be inspected by the DOL is correspondingly low.

Some studies have attempted to quantify the likelihood that high-risk employers may receive a DOL inspection. Daniel Galvin (2016) estimates that the probability that any given employer was investigated by the DOL WHD in 2012 was 0.5 percent, and that even in the most heavily targeted industries—retail, fast food, and janitorial services—the probability of an employer being inspected in

a given year did not reach 1 percent. Ji and Weil (2015) use the WHD inspection record over 2001 to 2005 to infer that, in fast food, the annual probability of any given establishment being inspected was less than 2 percent.

Since these estimates are from 2012 and from 2001–2005, respectively, they likely do not reflect improvements in DOL operations and resourcing over recent years, and therefore may be underestimates of the probability of detection facing firms today: the number of DOL WHD investigators was increased by 40 percent from 2009 to 2015 (Perez 2015), and the DOL has increasingly focused its investigations on the sectors and firms most likely to offend (which has likely significantly enhanced the effectiveness of its operations, as evidenced by the rise in the share of directed investigations that find violations (Weil 2018)).

Nonetheless, unless this increase in resources and targeting were able to increase probabilities of detection by more than an order of magnitude, the threat of a targeted DOL investigation alone seems unlikely to be enough to incentivize compliance for many firms under the existing penalty regime. As Weil (2010, p. 81) notes, “given that the probability of investigation in most industries is far below 10 percent, the theory of deterrence suggests that WHD penalty policies are far too low.”

Worker complaints cannot be relied on to surface minimum wage violations in many contexts

Another channel by which a firm can be caught violating federal minimum wage or overtime law is through worker complaints to the DOL. Given the scarcity of inspection resources and the large number of covered workers, this is a major channel on which enforcement relies in practice (Lott and Roberts 1995, Weil and Pyles 2005, Alexander and Prasad 2014, Clemens and Strain 2020). As of 2017, 50 percent of WHD investigations were complaint-led and 50 percent proactive (Weil 2018).²⁶ Nonetheless, for several important reasons enforcement strategy cannot and should not rely primarily on worker complaints to give firms an incentive to comply, particularly for the minimum wage.

First, many workers are unaware that the pay practices of their employer violate the law (Bobo 2011, Alexander and Prasad 2014). Workers may simply not know the law covering minimum wage or overtime. Or employers may violate the law in ways that are hard for workers to detect. These include requiring unpaid apprenticeships or training before hiring someone as a paid worker; making illegal deductions from paychecks, including deducting money from wages for workers’ mistakes (this is illegal if it brings the wage below the minimum); failing to give breaks or failing to pay for breaks not taken; requiring workers to stay before or after shifts without pay; failing to pay workers for driving time between jobs; misclassifying workers as exempt from overtime requirements; paying piece rates (for the job or by the day)

26 This represents a substantial shift toward targeted inspections in recent years: in 1998–2008 more than 75 percent of WHD investigations arose from worker complaints (Weil 2010). The DOL’s recent “strategic enforcement approach,” described in Weil (2018), aims to use the limited resources of the WHD most effectively by triaging complaints and increasing proactive investigations.

that do not amount to the federal hourly minimum wage or do not reach workers' statutory overtime pay; making workers pay to work (for example, for the right to earn tips); or misclassifying workers as independent contractors.²⁷

Second, workers may suspect that they have been underpaid, but lack any record of their hours to prove it (see, e.g., Dombrowski, Garcia, and Despard 2017). Or the “fissuring” of the workplace—the increased use of subcontracting and outsourcing of labor services, as well as independent contractors—may muddy workers' status as employees and/or obscure which company directly employs them, making it difficult for them to determine their rights (Weil 2018).

Third, even for those who are aware that they are being underpaid, many may be reluctant to complain. They may be scared of employer retaliation if they make a complaint,²⁸ or of losing their job if the firm is penalized by the DOL (Weil and Pyles 2005, Bernhardt et al. 2009, Alexander and Prasad 2014).²⁹ They may also be reluctant to complain to the federal authorities if they have other reasons to avoid the authorities, such as if they or someone in their family are undocumented (see, e.g., Fine 2006, Milkman et al. 2010, Fussell 2011, Grittner and Johnson 2021). Or, in high-turnover industries, they may simply move on and find another job if pursuing the old employer for the back wages is too time-consuming or complicated (Bobo 2011).³⁰ Finally, in some cases a firm and worker may collude to avoid paying the minimum wage, meaning that the worker will not want to complain to the DOL (Yaniv 1994, Clemens and Strain 2020).

These factors make it unsurprising that complaints are scarce and that, when they do come, they are often not from the most vulnerable workers. Weil and Amanda Pyles (2005) estimated, for example, that for every 130 overtime violations, only one complaint is received, and that the industries with the highest rate of FLSA complaints to the DOL are not those with the highest rates of violations. In addition, even if a worker does complain, the scarcity of WHD resources means that not all worker complaints are pursued (Weil 2018). And finally, because complaints have a positive externality—the individual worker's benefit from complaining is likely much lower than the overall social benefit, since other workers are likely also affected by the same violations—even in a world where workers were fully informed and not afraid of retaliation, complaints would be underprovided relative to an efficient scenario (Weil and Pyles 2005).

27 Many of these are described in detail in Bobo (2011) and Nir (2015).

28 In a survey of low-wage workers by Bernhardt et al. (2009), 43 percent of workers who had complained about a workplace issue reported having experienced employer or supervisor retaliation.

29 Weil and Pyles (2005) observe that “Public law groups and other organizations representing low-wage workers note that many employee complaints related to...the FLSA are filed after a worker has been fired by an employer...(thereby lowering the cost of complaining at that point).”

30 The presence of unions or other workplace advocacy groups can substantially lower barriers to worker complaints (Weil 2010). However, only 6 percent of private sector workers are unionized, and union density is even lower in many low-wage industries with high rates of wage theft (Hallett 2018).

Worker-initiated action through the courts has likely substantially increased firms' probability of detection in recent years, but is not a realistic avenue for many workers

The remaining FLSA enforcement channel is a worker pursuing the employer through the courts, either individually or as part of a collective action. The use of collective actions for FLSA wage and hour claims has grown rapidly: over 2013–19 an average of 7,900 cases were filed in federal court each year under the FLSA, compared to fewer than 2,000 in 2000 (Seyfarth Shaw 2020). This means that collective actions have rapidly become a meaningful complement to DOL enforcement action: the presence of collective actions appears to roughly double the probability of detection firms face.³¹ This has occurred despite the fact that the opt-in nature of collective actions under the FLSA makes it substantially more difficult (relative to other class actions) for a large group of workers to be assembled to bring a case of meaningful value against an employer (Ruckelshaus 2008, Becker and Strauss 2008).³²

However, as with individual complaints, collective action is not a realistic avenue for many workers, because of lack of information or awareness about the law, lack of time and resources to pursue a complaint, or fear of retaliation or job loss. Costs may also be an issue. When an employee brings an FLSA claim to court, she is often responsible for the costs of litigation upfront, and may remain liable for attorneys' fees if unsuccessful (Ruan 2012). Free legal services organizations have limited capacity to take on wage and hour cases (and federally funded legal services organizations are prohibited from serving undocumented workers). And while some plaintiff-side lawyers take cases on a no-win no-fee basis, this is often difficult in wage and hour cases for individual or small groups of low-wage workers because of low damage amounts (Becker and Strauss 2008, Lee 2014).

Moreover, the increased use of mandatory arbitration clauses and collective action waivers means far fewer workers can exercise the right to bring a claim against an employer for underpayment (Ruan 2012, Sternlight 2015, Colvin and Gough 2015, Estlund 2018). Alexander Colvin (2018) estimates that 56 percent of

31 Between 2004 and 2018 around 6,000–12,000 FLSA minimum wage or overtime cases were concluded by the DOL per year.

32 Unlike the majority of class actions, which operate under Federal Rule of Civil Procedure 23, class actions for federal minimum wage and hour violations are governed by the FLSA. The FLSA allows for class actions (called “collective actions”) on an opt-in basis for other similarly situated workers. In most other class actions, including those in consumer fraud, antitrust, or civil rights, membership of the class is opt-out (Ruan 2012). The opt-in nature of collective actions makes the formation of the class more difficult and reduces the likelihood of assembling a large class: in low-wage industries where workers frequently change jobs and move homes, even contacting putative class members can be difficult; workers receiving mailed notices to request an opt-in may not open them, or may not understand them; and many workers may be intimidated by the prospect of opting in to a lawsuit against an employer (Becker and Strauss 2008). In addition, filing a Rule 23 class action tolls the statute of limitations for all putative class members, whereas in a collective action under the FLSA, members are tolled only from the date they opt in, increasing firms' incentives to delay responding to claims and often reducing overall damages; and FLSA collective actions—in contrast to Rule 23 class actions—often require very large burdens of discovery (Becker and Strauss 2008). Many states have laws allowing workers to bring minimum wage or overtime class actions with an opt-out rather than opt-in format (Lurie 2011).

nonunion private sector employees are subject to mandatory arbitration clauses and 23 percent to class action waivers.

Together, this analysis of the different enforcement channels illustrates that for a large share of firms, the probability of detection they can expect to face if they underpay the minimum wage or overtime is likely substantially lower than the minimum threshold required to incentivize compliance. This is particularly likely to be true for firms with characteristics that make them less likely to be detected: firms with few workers (which makes it less likely both that they will be inspected and that a worker will complain), firms in high-turnover industries (which may go out of business in a few years), firms with a large share of vulnerable or dependent workers (who may be less likely to complain), or firms operating in the underground economy (Weil 2005).

State-level enforcement is important, but cannot be a substitute for strong federal protection

In the analysis in this paper, I have focused on the incentives created by the federal enforcement system. It is important to note that many states have minimum wage and overtime requirements that exceed the federal standard, and many states have stronger enforcement apparatus and larger penalties. Several states, for example, require treble damages in the case of minimum wage violations, and the District of Columbia in 2013 became the first jurisdiction to approve quadruple damages for unpaid wage claims (Hallett 2018)³³; others have a stronger record in criminal prosecutions of minimum wage violations and/or are more likely to levy civil monetary penalties.

On the other hand, many states do not have higher minimum wage or overtime standards than the FLSA sets out, and/or do not impose substantially higher penalties or provide enforcement resources over and above those of the federal system. For example, Alabama, Louisiana, Mississippi, South Carolina, and Tennessee have no state-level minimum wages, and fifteen additional states have state-level minimum wages equal to or less than the federal minimum wage.³⁴ Florida has a minimum wage law but lacks a state-level enforcement agency (Galvin 2016). Many states have stretched enforcement resources: Bobo (2011) reports that across the country, there are fewer than 1,000 state-level wage and hour enforcement staff, and more than half of the states have 15 or fewer enforcement staff; Schiller and DeCarlo (2010) identify fewer than 700 state-level wage and hour enforcement staff nationwide, with over half of states having fewer than 10 investigators. While these numbers represent a substantial increase over the 1,000 federal WHD investigators, they remain tiny relative to the number of workplaces where minimum wage or overtime violations might occur (Weil 2018). In addition, while some states carry out proactive investigations, most only undertake reactive enforcement in response to worker complaints (Lurie 2011,

33 This significantly reduces the probability of detection that even first-time violators would need to expect to incentivize compliance: treble damages mean firms must expect a 33 percent probability of detection to incentivize compliance, and quadruple damages require only a 25 percent probability of detection.

34 As per www.dol.gov/agencies/whd/mw-consolidated (accessed on June 1, 2021).

Meyer and Greenleaf 2011). And in some states, including Texas and Utah, the state enforcement agency enforces employment law violations only for workers *not* covered by the FLSA (Lurie 2011).³⁵

The varying patterns of state-level legal coverage and enforcement mean that the federal penalty and enforcement system is the main protection for a large share of US workers. In this paper I focus on the federal level not because state-level protections are unimportant, but because the federal level provides the baseline for workplace protections to avoid race-to-the-bottom dynamics between states and because for many millions of workers federal protection is the most relevant.

Evidence on Noncompliance with Minimum Wage and Overtime Laws

The analysis above suggests that many firms have little incentive to comply with minimum wage and overtime laws. It is therefore unsurprising that there is evidence of widespread noncompliance.

A survey of front-line workers in low-wage industries in Chicago, Los Angeles, and New York found that 68 percent experienced at least one pay-related violation of federal or state law in any given week, at an average cost of 15 percent of the affected workers' wages (Bernhardt et al. 2009). Estimates using data from the Current Population Survey indicate variously that 2.4 million workers in the 10 most populous states are underpaid by an average of 25 percent of their weekly wages as a result of federal or state-level minimum wage violations (Cooper and Kroeger 2017); that 560,000 workers in New York and California experienced a minimum wage violation in any given week in 2011, with losses amounting to 37–49 percent of their income (Eastern Research Group 2014); and that 16.9 percent of low-wage workers in the United States experienced a minimum wage violation in 2013, losing on average 23 percent of their earnings (Galvin 2016).³⁶ Clemens and Strain (2020) find that minimum wage noncompliance increases when minimum wages are raised, estimating that increases in measured underpayment following minimum wage increases average between 10 and 25 percent of realized wage gains.

Some of the best evidence on the prevalence of noncompliance in specific high-risk sectors comes from random inspections. Weil (2005) found that, in a random inspection of apparel contractors in 2000, more than half were not in compliance with the minimum wage provisions of the FLSA and a typical contractor owed about \$3,700 in back wages. He also reports that DOL investigations of the top 20 fast food outlets over 2001–05 found 40 percent of them in violation of the FLSA minimum wage or overtime provisions (Weil 2010). And more recently, random DOL WHD inspections of the garment industry in 2015 and 2016 found violations at 85 percent of workplaces (Weil 2018).

35 In addition, even in states with substantial enforcement, the degree to which workers actually receive the back wages owed to them varies: a Politico investigation of 15 states found that on average 41 percent of the back wages that firms are ordered to pay as a result of minimum wage violations were not paid to workers (Levine 2018).

36 Further evidence on the prevalence of minimum wage and overtime noncompliance is reviewed in Ruckelshaus (2008) and Bobo (2011).

The value of the income lost to minimum wage and overtime underpayments is large. David Cooper and Teresa Kroeger (2017) estimate that minimum wage underpayments alone, in the 10 most populous states, total \$8 billion per year, and the Eastern Research Group's (2014) estimates imply that minimum wage underpayments in California and New York amount to about \$1.7 billion per year. But recoveries by the enforcement system are a fraction of the estimated volume of underpayment. The DOL recovered an average of around \$280 million in unpaid wages each year for the last five years,³⁷ and Celine McNicholas, Zane Mokhiber, and Adam Chaikof (2017) estimate that the entire enforcement system—the DOL, state enforcement agencies, and class action settlements—recovered an average of \$1 billion per year in 2015–16 in underpayments resulting from minimum wage and overtime violations, off-the-clock and meal break violations, illegal deductions, and employee misclassification. The disparity between the amount underpaid by employers and the amount recovered by the enforcement system reinforces the conclusion that increased deterrence is vital to reduce underpayment.

Finally, it should be emphasized that wage and hour violations disproportionately affect the most vulnerable workers: violation rates are significantly higher for nonwhites and noncitizens (Galvin 2016), and undocumented workers suffer violations at high rates but rarely receive relief (Bobo 2011).³⁸

3. ORGANIZED LABOR, UNFAIR LABOR PRACTICES, AND THE NLRA

The National Labor Relations Act guarantees workers' rights to organize in a union, bargain collectively, and strike, among other things. Yet there is no meaningful legal penalty for employers that do not respect these rights. This is because, when enforcing the NLRA, the National Labor Relations Board is permitted to seek only "make-whole" remedies—remedies that compensate employees for losses incurred as a result of the employers' practices (to "make them whole")—and informational remedies. There is no legal scope to subject companies to any financial penalties for violations of laws protecting organized labor, and there is no criminal liability. Table 4 lists some of the key provisions of the NLRA with respect to labor organizing, and the associated penalties.³⁹

37 According to the DOL website: <https://www.dol.gov/agencies/whd/data> (accessed on May 30, 2021).

38 More broadly, Marinescu, Qiu, and Sojourner (2020) document that labor and employment violations across a range of categories (including overtime violations) disproportionately fall on lower-paid workers.

39 If the NLRB finds "flagrant or egregious" violations, it can order "extraordinary remedies" in addition to those listed in table 4. These may include requiring the employer to mail the NLRB's orders directly to each employee's home or granting the union access to the employer's premises to post notices or meet with employees on nonwork time. The NLRB may also require the employer to pay litigation costs, attorney's fees, and union expenses, though the possible magnitude and scope of these awards is disputed.

Table 4
NLRA-prohibited employer behaviors and remedies

Section	Prohibited behavior	Possible NLRB remedies if employer is found to be noncompliant
8(a)(1)	Interfering with, restraining, or coercing employees in their rights to organize in a union or collectively bargain	Issue a cease-and-desist order. Post a notice at the premises. If the employer is found to have interfered with a union election process, the NLRB may issue a bargaining order: the election is stopped and the employer must bargain with the union.
8(a)(2)	Dominating or controlling a union	Issue a cease-and-desist order. Post a notice at the premises. Order to cease interfering with the union. Order the union to be disbanded. Require employer to repay union dues withheld from employee paychecks.
8(a)(3)	Discharging or otherwise discriminating against an employee because of their union activities or sympathies	Issue a cease-and-desist order. Post a violation notice at the premises. Require reinstatement of discharged employee(s) and back pay (net of any earnings the employee(s) received in the interim).
8(a)(4)	Discharging or otherwise discriminating against an employee for filing charges or giving testimony to the NLRB	Issue a cease-and-desist order. Post a notice of violation on the premises. Require reinstatement of discharged employee(s) and back pay (net of any earnings the employee(s) received in the interim).
8(a)(5)	Failing to bargain in good faith with the union	Issue a cease-and-desist order. Post a notice at the premises. Direct employer to resume bargaining in good faith.

NLRA = National Labor Relations Act; NLRB = National Labor Relations Board

Incentives to Commit Unfair Labor Practices

Because the NLRA can only issue make-whole and informational remedies, it is extremely unlikely that the costs of noncompliance will outweigh the benefits for employers. Indeed, in a detailed analysis of firms' incentives to comply with the NLRA, Morris Kleiner and Weil (2012, p. 48) conclude that the expected costs of noncompliance "represent a fraction of the benefits to employers...from thwarting organizing drives."

In this section, I build on Kleiner and Weil's (2012) analysis to calculate a rough estimate of the financial cost-benefit trade-off firms face when deciding whether to comply with NLRA Section 8(a) provisions on unfair labor practices. While the calculation is not as straightforward as for minimum wage and overtime violations—where the benefit to the firm of noncompliance can be approximated roughly by the value of unpaid wages—this calculation gives a

sense of the vastly disproportionate incentives firms face to break labor law. I specifically consider violations under Sections 8(a)(3) and 8(a)(4), which cover dismissal of an employee for “union activities or sympathies” or for filing charges or giving testimony to the NLRB. These are the most commonly violated aspects of the NLRA: over 2000–09, they accounted for 65 percent of all violations by employers detected by the NLRB (Kleiner and Weil 2012).

Why might a firm decide to fire an employee (illegally) for union organizing activities? The dismissal of an employee for their union organizing activities may reduce the probability of a union successfully forming at the firm (and to dissuade workers from organizing, the firm does not need to dismiss *all* supportive workers, only enough workers to deter others from organizing.) Unionization can reduce firm profits, giving shareholders—and therefore management, if they are acting to maximize shareholder value—the incentive to avoid unionization.⁴⁰ In the most comprehensive paper to estimate the effect of unionization on firm profits in the United States, Lee and Mas (2012) estimate a 10 percent average decline in firms’ market value after unionization, equivalent to about \$40,500 per unionized worker in 1998 dollars (about \$60,000 in 2020 dollars, adjusting with the chained PCE price index).⁴¹ This implies that the average profit-maximizing firm may be willing to spend up to 10 percent of its total market value (\$60,000 per worker) to avoid unionization with certainty; alternatively, it should be willing to spend 0.1 percent of its market value, or \$600 per worker, to reduce the probability of unionization by only 1 percent.

For a typical firm, firing a worker for union activities may be profit-maximizing if it reduces the probability of unionization by as little as 0.15 percent

The Lee and Mas (2012) estimate of profits lost as a result of unionization can be used in a simple back-of-the-envelope calculation of the incentives for firms to dismiss workers unfairly. As a baseline, consider a nonunion firm with 500 workers who would be eligible to join a union.⁴² One of the firm’s employees is a prominent organizer for the union, and this employee receives the national average hourly compensation and works full-time (40 hours/week).⁴³ Assume that the

40 Note that a negative impact of unionization on profits does not necessarily imply a negative impact on output or productivity. Part of the purpose of a union is to redistribute the proceeds of production away from shareholders and toward workers. As Lee and Mas (2012, p. 337) note, “According to our calculations, if unionization represented a one-to-one transfer from investors to workers through higher wages, this magnitude would be in line with a union wage premium of 10%.... [This is] on the low side of union/nonunion differentials.” That is, their estimate of the reduction of firm profits as a result of unionization could be consistent with a permanent transfer of those profits to workers in the form of higher wages, implying zero (or even, possibly, positive) effects of unions on firm productivity.

41 In contrast, regression discontinuity designs comparing close union victories to close union losses (Lee and Mas 2012, DiNardo and Lee 2004) find no evidence of a close union win on stock market returns. Lee and Mas (2012) argue that these analyses can only estimate the average treatment effect for firms whose election was ex ante predicted to be close, which are a highly selected sample.

42 This is approximately the average number of eligible workers in a given firm in NLRB elections over 1961–99 in the sample considered by Lee and Mas (2012).

43 The average cost to the employer of employee compensation, per hour worked, in the United States in September 2020 was \$38.26, according to the Bureau of Labor Statistics’ Employer Costs for Employee Compensation data set.

firm expects that, if it illegally dismisses the union organizer, it will be certain to be detected and penalized by the NLRB. This is a conservative assumption: while Kleiner and Weil (2012) argue the probability of an NLRA violation being detected is substantially higher than for other violations of workplace laws, and could be close to 100 percent (because of unions' role in the process), Bronfenbrenner's (2009) research suggests that in many cases even if an employer behaves illegally in a union organizing campaign, no unfair labor practice claim is brought to the NLRB.⁴⁴ Assume in addition that the firm will have to pay six months' worth of back wages to the dismissed worker when its violation is detected. This is also a conservative assumption: workers are only eligible to receive back pay *minus* any earnings from employment in the interim, so this calculation assumes the dismissed worker was unemployed for six months without any other employment earnings.⁴⁵ Finally, assume that the firm will have to hire a replacement worker, at the national average cost-per-hire of \$4,425 (SHRM 2017). In this scenario, the expected cost to the firm of dismissing the union organizer is \$44,215.40.⁴⁶

What assumptions about the expected benefits of dismissal are necessary to make this a profit-maximizing decision on the part of the firm? The expected benefit of dismissing the union organizer must be greater than or equal to \$44,215.40. Taking the Lee-Mas (2012) estimates of the cost to firms' market value of unionization, our baseline firm's shareholders would experience a loss of \$30 million (\$60,000 * 500) if the union successfully organized. This means that, from the firm's profit-maximizing perspective, there is an incentive to fire a worker illegally if doing so reduces the chance of a successful union organizing effort by only 0.15 percent. (And if the chance of the illegal firing being detected and penalized by the NLRB is less than 100 percent, this threshold is reduced still further).

More broadly, the incentive for a firm to dismiss a worker illegally depends on a number of factors:

- the probability that a charge of unfair dismissal will be brought to the NLRB and upheld,

44 Bronfenbrenner's (2009) comparisons of organizer-reported unfair labor practices (recorded in surveys), with NLRB unfair labor practice (ULP) data, show that "less than half of all illegal employer violations [are] captured by ULPs". This can be because there is little incentive for workers to pursue this (as it can be time-intensive, and the financial relief available can be small), and/or because workers are afraid of retribution from their employer, particularly in the cases of organizing campaigns which were lost.

45 In addition, Brudney (2010) estimates that 43 percent of employees who received back pay through NLRB orders got less than the amount those workers' case files would indicate would fully compensate them for the earnings loss.

46 This represents paying 6 months' worth of back pay (\$39,790.40 = \$38.26 hourly compensation cost * 40 hours * 26 weeks) plus paying the fixed cost of hiring a replacement worker (\$4,425). Kleiner and Weil (2012), using data on NLRA violations from 2000–09, show that the mean dollar value of back pay awarded per individual for violation of Section 8(a)(3) was \$10,956, and the mean dollar value of back pay awarded for violations of Section 8(a)(4) was \$15,904. Analysis of the NLRB's public data on the board's website, covering 2010–19, shows that the average value of back pay received by workers, divided by the number of workers offered reinstatement, was \$35,730 over this period (although this is not directly comparable to Kleiner and Weil's (2012) figures because the data are not broken out by the applicable section of the NLRA). Together, these suggest that my estimate of the average cost of unfairly dismissing a worker may be somewhat of an overestimate, meaning that firms may have an even stronger incentive to unfairly dismiss a worker in practice.

- the back wages owed to the worker in question (noting that any employment income the worker, has earned during this time is subtracted from the back wages owed),
- the cost of hiring a new worker to replace the dismissed worker, and
- the expected loss of firm profits as a result of unionization.

How do these factors affect firms' incentive to dismiss workers illegally? Figure 5 illustrates firms' incentive to dismiss a worker illegally under different assumptions about the expected loss of firm profits as a result of unionization (on the x-axis) and the expected cost of firing the worker (based on different assumptions about the chance of detection and the number of months' back wages to be paid for the average full-time full-year worker). The y-axis value for each point indicates that, under these assumptions, a profit-maximizing firm would have an incentive to fire a worker illegally if this would reduce the probability of a union forming by y percentage points.

Figure 5

“Threshold probability”—the degree to which firing a worker will reduce the chance of unionization—which would give firms an incentive to break labor law by firing a worker illegally, under different assumptions about the expected (1) loss of profits from unionization and (2) cost of the illegal firing

Firm has an incentive to fire a worker if dismissal reduces chance of unionization by at least...



Source: Author's calculations.

The light blue line in the figure illustrates that even if the firm's violation is certain to be detected, and if it will have to pay six months' worth of back wages as compensation, a firm standing to lose \$2 million in profits has an incentive to fire a worker illegally if that firing reduces the probability of unionization by around 2.2 percent; a firm standing to lose \$10 million in profits has an incentive to fire a worker illegally if doing so reduces the probability of unionization by 0.44 percent;

and the average firm studied by Lee and Mas (2012), which lost \$30 million in equity value after a unionization election (as expressed in 2020 dollars, adjusted for inflation), had an incentive to fire a worker illegally if that firing would have reduced the probability of unionization by only 0.15 percent (as detailed above).

This exercise is in a similar spirit as that conducted by Kleiner and Weil (2012). They analyze the expected benefit to an employer of committing an unfair labor practice during a union organizing campaign. Using the same Lee and Mas (2012) estimates of the expected loss in firm profits as a result of unionization, they calculate that for a firm with 100 workers in the bargaining unit, the total cost to shareholders of a unionized workforce would be \$4 million. They estimate that committing an unfair labor practice can reduce the probability of a union election win by 10 percent, and they use a value of \$54,000 for the expected cost to the employer of violating the NLRA. With these parameters, the net benefit for a typical firm of committing an unfair labor practice is around \$400,000 (a 10 percent reduction in the chance of a loss of firm equity value of \$4 million), and the expected cost is \$54,000—giving firms a very strong incentive to commit unfair labor practices in the hope of thwarting a union organizing drive. In this scenario the firm would have an incentive to commit an unfair labor practice if this reduced the probability of a successful union organizing campaign by only 1.4 percent.⁴⁷

What is the effect of an unfair labor practice on the probability of a successful union organizing drive? John-Paul Ferguson (2008) attempts to answer this question by studying records of organizing drives that filed an NLRB petition over 1999–2004. Of 22,382 such petitions in this period, 3,180 organizing drives reached a first contract within one year of certification. Ferguson finds that the filing of any unfair labor practice charge was associated with a 25 percent lower chance of an election being held and a 13 percent lower chance of a contract being reached within one year of a successful union election.⁴⁸ While the exact degree to which these estimates can be interpreted as causal is unclear, they are between *one and two orders of magnitude larger* than the probabilities which give firms an incentive to violate the NLRA. That is, under any reasonable assumption about the degree to which firing workers illegally can reduce the probability of unionization, a large number of firms have a financial incentive to do so.

Finally, note that while undocumented workers are protected by the NLRA, they do not have access to the back pay remedy (Block and Sachs 2020). This means that there is close to zero financial cost for firms that fire undocumented workers to prevent union organizing.

Together, these exercises illustrate that the financial penalties for unfair dismissal of workers for union organizing are far outweighed by the potential benefits to firms of avoiding unionization.

47 This is calculated as the expected cost of violation (\$54,000) divided by the expected benefit of violation (i.e. expected cost of unionization of \$4 million). The fact that probability here is higher than my initial estimate of 0.15 percent is driven partly by a smaller bargaining unit (meaning the expected total cost of unionization to shareholders is lower), and partly by a higher expected cost of a violation.

48 Similarly, Freeman (1986) finds that in years with a larger number of unfair labor practices per election, a smaller share of workers in a given industry won the right to union representation (controlling for year fixed effects, industry fixed effects, wages, producer prices, and profits). Dickens (1983) finds that employer threats and antiunion campaigns have a significant effect on union election outcomes.

Many other sources have noted the lack of legal incentive for firms to comply with the NLRA. John Schmitt and Ben Zipperer (2009, p. 2), for example, note that “Given these small penalties for illegal firings, the NLRA, in practice, has given employers a powerful anti-union strategy: fire one or more prominent pro-union employees...with the hope of disrupting the internal workings of the union’s campaign, while intimidating the rest of the potential bargaining unit.” Lance Compa (2004, p. 68) writes that “In practice, many discriminatory discharge cases are settled with a small back-pay payment and workers’ agreement not to return to the workplace. At a modest cost and with whatever minor embarrassment comes with posting a notice, the employer is rid of the most active union supporters, and the organizing campaign is stymied.”⁴⁹

The incentives to comply with the other provisions of the NLRA are similarly weak. As shown in table 4, if an employer is found not to have bargained in good faith with the union, the NLRB can only direct the employer to resume bargaining in good faith—and in some cases, require the union’s costs to be paid (Garrett 2016). If the employer is found to have interfered with, restrained, or coerced employees in their rights to organize or collectively bargain, the NLRB can order this to stop, a notice to be posted, and in some cases can issue a bargaining order requiring the employer to bargain directly with the union. In neither case can the NLRB levy financial penalties on the employer.

Evidence of Noncompliance

As one would expect given the weak incentives, there is evidence of widespread employer noncompliance with labor laws (along with the use of a variety of lawful strategies to suppress union organizing). Kate Bronfenbrenner (2009), for example, studied a random sample of 1,004 NLRB unionization elections that took place over 1999–2003 and found that 40 percent of them involved at least one unfair labor practice charge brought by the union. Based on detailed interviews with union organizers, she found that at least 75 percent of the employers in the sample were alleged to have carried out at least one illegal action, including 34 percent of employers alleged to have discharged union activists.⁵⁰ Celine McNicholas and colleagues (2019) studied all the NLRB representation elections in 2016 and 2017 and found similarly that unfair labor practice charges were filed against employers in over 40 percent of these elections, and that in 20–30 percent of the elections an employer was charged with illegally firing a worker.

49 Freeman and Kleiner (1990) also provide evidence consistent with firms responding to financial incentives when making NLRA compliance decisions. Specifically, they find that firms where the potential union compensation differential was larger (i.e. the potential effect of unionization on profits was larger) were more likely to have had unfair labor practice charges filed against them in the context of a union election. This would be consistent with firms being more likely to try to deter unionization by committing unfair labor practices when unionization would be more costly in terms of reduced profits.

50 The disparity between the number of elections in which union organizers allege illegal practices and the (much smaller) number in which an unfair labor practice charge was filed is not necessarily surprising: given the low potential for restitution even for the serious charge of dismissing a union organizer, the costs in money and time of bringing a case, and employees’ fear of retaliation, the incentive to bring unfair labor practice charge cases is often limited (Bronfenbrenner 2009).

Schmitt and Zipperer (2009) use data from NLRB elections to estimate the probability that workers are illegally fired in connection with a union election. They estimate that over 2001–07, one in four NLRB elections featured at least one illegal firing. Using a method developed by Paul Weiler (1983) and Robert LaLonde and Bernard Meltzer (1991), they estimate that the probability that *any* prounion worker would be fired in a union election campaign was around 1 in 52; or, alternatively, assuming that 10 percent of prounion workers are union activists (who are most likely to be targeted by employers) they estimate that one in five union organizers or activists can expect to be fired during a union organizing campaign.

Kleiner and Weil (2012) calculate an alternative metric of employer opposition to union organizing: the ratio of unfairly dismissed workers offered reinstatement by the NLRB to the number of workers voting for unions in NLRB elections. In the 1950s, roughly 1 worker was unfairly dismissed and offered reinstatement during union organizing campaigns, for every 200 workers that voted to form a union; by the 1980s, 9 workers were unfairly dismissed and offered reinstatement for every 200 workers that voted to form a union. Over the past decade, 10 workers have been offered reinstatement by the NLRB for every 200 workers voting to form a union in certification elections.⁵¹

Lynn Rhinehart, Lane Windham, and Lawrence Mishel (2020) present evidence that strategic violation of labor law became a common practice for firms seeking to avoid unionization by the 1970s and 1980s. For example, they write that a frequent contributor to Harvard Business School case studies in the 1980s instructed that since the NLRB process for dealing with unfair labor practices was lengthy and the penalties “quite mild,” “it is quite possible for management to effectively destroy an organizing effort or, at the very least, signal to employees the relative ineffectiveness of the union in dealing with management”, and that one California State University business professor argued that “In all but the most unusual circumstances it is almost negligent for a company to allow unionization to happen.... When one surveys all the things a nonunion employer can do to stay that way...the employer would almost have to try to get itself organized to end up with a union” (Rhinehart, Windham, and Mishel, 2020, p. 24).⁵²

The strong economic incentive for employers to oppose union organizing efforts presents a plausible explanation for the “voice gap” in US workplaces: the large disparity between union membership rates and the rates at which workers report a desire to join a union (Kleiner and Weil 2012). The union membership rate for wage and salaried workers has declined consistently over recent decades, reaching a low of 11.6 percent in 2019 overall and 6 percent in the private sector (Hirsch and Macpherson 2003, updated March 2021).⁵³ Meanwhile, Thomas Kochan and colleagues (2019) found in a 2017 survey that almost half

51 Kleiner and Weil’s calculations end in 2009. Using 2011–19 data from NLRB annual reports on the number of reinstatements offered and the number of workers voting for the union in certification elections, I calculate a ratio of 10:200 on average over the period.

52 These examples were originally from William E. Fulmer’s 1982 book *Union Organizing: Management and Labor Conflict* and John G. Kilgour’s 1981 book *Preventive Labor Relations*, respectively.

53 This compares to a peak private sector union membership rate of around one third in the 1950s (Rosenfeld 2014).

of nonunion workers would vote to join a union; similarly, Richard Freeman (2007) reported from a 2005 survey that more than 50 percent of nonunion workers would “definitely or probably vote for forming a union” in a union representation election.

4. WHAT CAN BE DONE? INCREASING INCENTIVES TO COMPLY

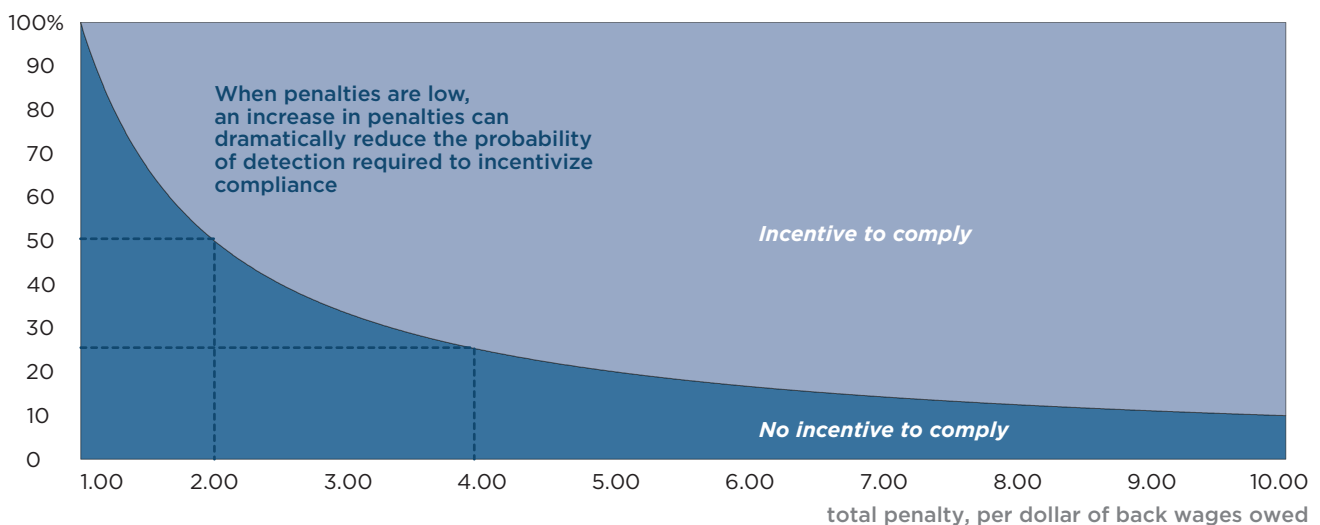
Minimum Wage, Overtime, and the FLSA

While the FLSA provides for the possibility of relatively large penalties—not only payment of back wages to workers but also liquidated damages, civil monetary penalties, and criminal sanctions for serious willful offenses—the DOL data examined in this paper suggest that the actual financial costs to firms that violate FLSA minimum wage and overtime provisions are mostly small. In turn, since most violating firms can expect to face relatively small costs if detected, many firms would have to expect near certain detection to have an incentive to comply with FLSA wage and hour laws. As noted by Nicole Hallett (2018, p. 119): “Given this reality, the wage theft crisis is less surprising than the fact that any employer decides to comply with the law at all.”⁵⁴

Incentives to comply can be strengthened by a combination of increasing average penalties and increasing the probability of detection, as illustrated in figure 6. The two need to be deployed in tandem to create an effective deterrent: the expected penalty must rise exponentially as the probability of detection declines (Weil 2010).

Figure 6
Combinations of probability of detection and expected penalty which generate an incentive to comply

Probability of detection



Source: Author's calculations.

54 A 2018 Politico investigation (Levine 2018) quotes Richard Blum, a staff attorney at the Legal Aid Society in New York, as saying that employers make strategic decisions to violate wage laws: “It is competitively smart to cheat and steal from your workers because the odds of getting caught are low and the odds of having to pay are low.”

The probability of detection can be increased in several ways. Allocation of more federal staff and resources for proactive inspections would substantially increase the likelihood that a violation is detected by a DOL investigation, as would further increases in the use of strategic deterrence-based enforcement approaches (Levine, Toffel, and Johnson 2012; Weil 2010, 2018) and increased cooperation with worker advocacy organizations like worker centers (Fine and Gordon 2010, Weil 2010, Fine 2017). Probabilities of detection of wage and hour violations *outside* the DOL can also be raised by reducing barriers for workers to bring collective action cases under the FLSA, for example by changing the opt-in standard to an opt-out standard as in other (Rule 23) class actions, and by reducing the prevalence of mandatory arbitration clauses and class action waivers in employment contracts (Becker and Strauss 2008, Ruan 2012).

However, given the current penalty regime, it is questionable whether the probability of detection could ever feasibly rise to the levels needed to ensure that all (or most) firms have an incentive to comply. As the calculations in this paper indicate, current penalties for typical firms mean that most firms need to expect a 78–88 percent chance of detection to have an incentive to comply with the FLSA. The scale of inspection resources that would be needed in order that all firms operating in the low-wage labor market believe they face a 78–88 percent chance of detection would likely be very large (perhaps infeasibly large), particularly since these violations are often hard for employees to detect and/or employees are often unwilling or unable to report them. Higher probabilities of detection are therefore necessary but not sufficient to generate meaningful compliance incentives.

This means that substantially higher expected penalties are also central to improved minimum wage and overtime enforcement. Indeed, evidence shows that firms respond to the incentives a stronger penalty regime creates. Galvin (2016) measures the strength of state penalty and enforcement regimes across several dimensions and finds that states with higher penalties for minimum wage violations see lower rates of noncompliance. This is true particularly in states with treble damages and those with higher civil or criminal penalties.

How can expected penalties be increased? In any penalty regime, a balance needs to be struck between creating a deterrent and ensuring fairness and proportionality. The following strategies are at least in principle available under current law, and seem plausibly fair and proportional in terms of targeting more serious and/or clearly intentional violations:

- ensure that liquidated damages are always levied,
- substantially increase civil monetary penalties for willful and repeat violations,
- extend the statute of limitations for willful and/or repeat violations,
- use the “hot goods” provision across as many industries as possible, and
- substantially increase the use of criminal prosecution.

When considering fairness and proportionality, it is also illustrative to note that the penalties firms face for underpaying workers—wage theft—are far smaller than the penalties individuals face for theft. In every state, shoplifting goods worth \$2,500 or more can lead to felony charges and imprisonment

(Traub 2017). The contrast for wage theft of that amount is stark. The DOL detected more than 66,000 FLSA minimum wage or overtime violations over 2005–16 that resulted in \$2,500 or more in employee underpayment; the total value of back wages in these cases was \$1.9 billion. Of these, 2,672 violations were deemed to be willful, and the total value of back wages owed in these cases was \$145.7 million. Yet during this period there were only 10 criminal convictions under FLSA minimum wage or overtime provisions. In other words, there was no criminal penalty for the overwhelming majority of cases of wage theft, even when the amount workers were owed was large.

Ensuring that firms have a strong incentive to comply with the minimum wage will become even more important in the context of proposals to raise the federal minimum wage to \$15. The higher the minimum wage, the larger the number of workers covered and the greater the financial incentive for firms to avoid compliance.⁵⁵ With the existing penalty regime, there is a substantial risk that the increase in the federal minimum wage will fail to translate into large increases in take-home pay for many workers unless penalties and enforcement are systematically strengthened to ensure that workers receive the pay they are legally owed.

Labor Organizing Protections and the NLRA

The cost-benefit trade-off for employers considering violating the NLRA is even starker than for the FLSA. Sanctions on firms that commit unfair labor practices in the course of an employee organizing drive are almost always negligible, particularly when compared against the possibly large financial benefit to shareholders of avoiding unionization. Even the offense with the largest potential sanction—dismissal of a worker for union organizing—carries a maximum penalty of having to reinstate the worker with back pay. My estimates in this paper suggest that for an average firm, even if firing a union organizer would reduce the probability of unionization by less than 2 percent, and perhaps by as little as 0.15 percent, it would be financially worthwhile to do so.

It is therefore no surprise that so many firms are found to have fired workers during union organizing drives, and that workers worry about being fired if they try to organize a union. Indeed, Kim Bobo (2011, p. 1766), founding director of Interfaith Worker Justice, reported that “Whenever I am speaking with a group about unions, I always ask, ‘What would happen if you tried to organize a union at your workplace?’ Every single time the response is the same: ‘I would get fired.’”

The lack of incentive for employers to comply with the NLRA has been evident for some time. The Dunlop Commission (1994), for example, argued that the low penalty was a major cause of the increase in the NLRA violation rate (see also Kleiner 2001), and there have been repeated legislative attempts to increase penalties for unfair labor practices. As noted by Kleiner and Weil (2012, p. 49), “given the absence of any appreciable deterrence measure...it should...come as no surprise that the Act for decades has been ineffective in curbing behaviors that are antithetical to its fundamental aims.”

⁵⁵ Clemens and Strain (2020) find evidence that higher minimum wages increase the prevalence of workers paid wage rates below the minimum wage.

What can be done to reduce firms' incentives to commit unfair labor practices? Since the NLRA does not allow for any remedies other than "make-whole" remedies, it seems extremely unlikely that meaningful incentives to comply can be created through the existing legal framework: even if firms' violations are certain to be detected, it is often financially worthwhile to break the law because the penalties are so small relative to the potential benefits to profits from avoiding unionization.

As such, to ensure that firms have an incentive to comply with labor organizing protections it is necessary to increase penalties significantly. The Protecting the Right to Organize (PRO) Act,⁵⁶ which passed the House of Representatives in March 2021 and was featured in President Biden's 2020 election platform, would substantially increase the financial disincentive for employers to engage in unfair labor practices. It expands remedies to include back pay owed to employees *without* any reduction for interim earnings, as well as an equal amount in liquidated damages, and the possibility of consequential and punitive damages in accordance with the gravity of the offense and the income of the employer. In addition, the PRO Act would introduce civil monetary penalties for unfair labor practice violations up to \$50,000 per violation (or up to \$100,000 for violators who have committed a similar offense within the previous five years).

The act is clearly an important improvement on the status quo. However, the fact that for many firms the current financial incentives overwhelmingly favor unfair labor practices means that even a doubling of the expected penalties (from having only to pay back wages to having to pay back wages plus liquidated damages, for example) may not have a major impact on the cost-benefit trade-off. The extent to which the PRO Act would in practice affect employers' incentives to comply will therefore depend most heavily on two discretionary factors: the degree to which civil monetary penalties are levied and the degree to which punitive damages are awarded.

Beyond the PRO Act, there are several options for meaningfully increasing potential costs for firms that commit willful or repeated violations of labor and wage laws. They could include automatic multiyear debarment from federal contracts and the imposition of personal liability for company executives in the case of serious violations.

The "Fissured" Workplace

In this paper, I have focused on the financial incentives for employers to comply with the FLSA and NLRA in a typical employer-employee relationship. But attempts to increase firms' compliance incentives will be successful only if they also address the issues raised by the 'fissuring' of the workplace. In a fissured workplace (Weil 2014a), a large share of workers are not employed directly by the company for which they perform work, but instead by a subcontracting firm or staffing agency (especially in the cleaning, food service, and security sectors), or by franchisees of a brand management company (especially in hotels and fast food). There is extensive evidence that these employment structures increase noncompliance with labor and employment laws, as well as making detection

56 See <https://www.congress.gov/bill/117th-congress/house-bill/842>.

of this noncompliance more difficult (summarized in Weil 2010).⁵⁷ In addition, fissuring means that a growing number of low-wage workers are misclassified as independent contractors. Since firms are not required to pay independent contractors minimum wage or overtime, and independent contractors are not legally permitted to bargain collectively with their employer, this misclassification can often result in labor and employment law violations that workers themselves may not be aware of. While the creation of fissured employment structures is partly a response to changing economic and technological conditions, in many cases the incentive for firms to adopt these structures appears to be an increased ability to subvert labor law—or at least to reduce employment costs by turning a blind eye to labor law noncompliance (Ruckelshaus 2008; Zatz 2008; Weil 2010, 2014).⁵⁸

Ensuring that the incentives to comply with the FLSA and NLRA apply across the boundaries of these fissured workplaces is an extremely important aspect of guaranteeing labor protections in the modern workplace. The Department of Labor has taken several steps to address noncompliance in the fissured workplace (Weil 2018), enacting a proactive strategic enforcement approach focused explicitly on industry structure (see, e.g., Weil 2010, 2011). While a detailed examination of how to make further progress on enforcement in the fissured workplace is beyond the scope of this paper, addressing this issue could include an expansion of the definition of a joint employer, third-party liability for labor and employment violations, a clampdown on the misclassification of employees as independent contractors, a more expansive definition of the employment relationship (such as the ABC test for independent contracting status), explicit extension of labor and employment protections to workers regardless of their legal status, and the use of antitrust to align firms' span of control with their responsibilities under labor and employment law (see, e.g., Zatz 2008, Rogers 2010, Paul 2019, Block and Sachs 2020, Goldman and Weil 2020). Without addressing the fissuring of the workplace, increased incentives to comply with the minimum wage or union organizing protections may simply increase firms' incentive to 'fissure' their employment relationship to avoid legal liability—rather than increasing firms' incentive to comply with the law itself.

57 Companies at the bottom end of fissured employment structures often face small margins and fierce cost competition, increasing incentives to violate labor and employment law. At the same time, the expected costs of violations may be lower for such firms: they may face a lower probability of inspection and are likely to face less reputational cost than "lead firms" if found to have violated employment or labor law. Finally, penalties for repeat violations may induce companies at the bottom of fissured employment structures to simply shut down and reopen as a different firm (a strategy referred to as "phoenixing" in the UK labor market), a strategy that is much less attractive to large firms with well-established brands, capital equipment, and other workers.

58 In addition, even where the 'fissuring' of the workplace does not lead to explicitly illegal behavior, it is an increasing concern that these structures—in particular, the classification of workers as independent contractors—violate the spirit and intent of laws designed to provide workers with the right to minimum wages, overtime pay, and collective bargaining: in many cases, the degree of control the firm exerts over workers who are not their direct employees is large, while the legal responsibility the firm bears for these workers is small (Goldman and Weil 2020; Paul 2019, 2020).

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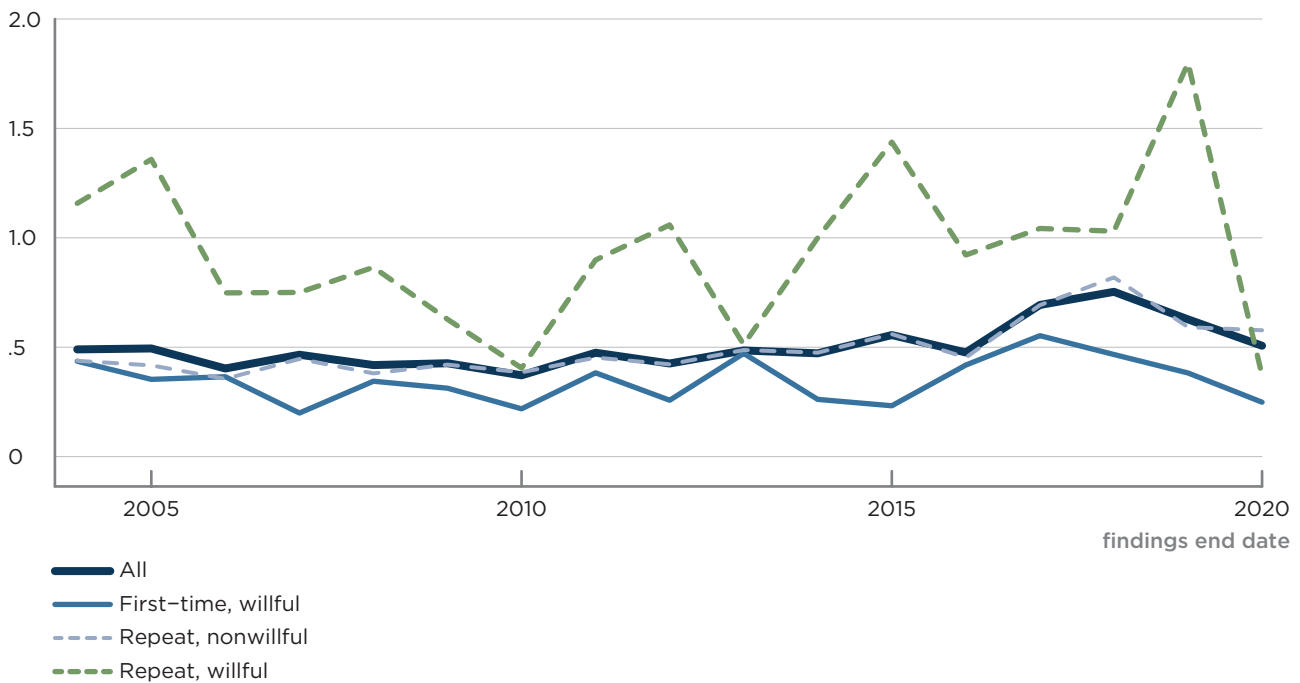
APPENDIX

This appendix shows average civil monetary penalty per dollar of back wages for repeat and willful violations of the FLSA (figure A1) and the distribution of civil monetary penalties for repeat and/or willful violators (figure A2) from 2005 to 2020.

Figure A1

Average civil monetary penalty (CMP) per dollar of back wages for repeat and willful violations of the FLSA, concluded DOL Wage and Hour Division actions, 2005-20

average CMP per dollar of back wages (dollars)



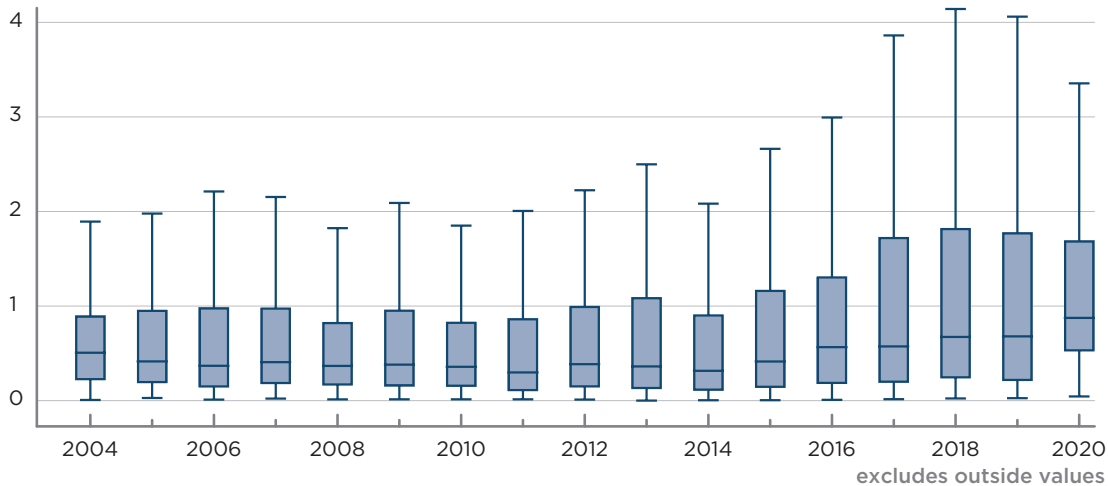
Note: "Findings end date" is the latest date in which the Department of Labor (DOL) found violations, not the year the investigation was concluded.

Source: Department of Labor WHISARD.

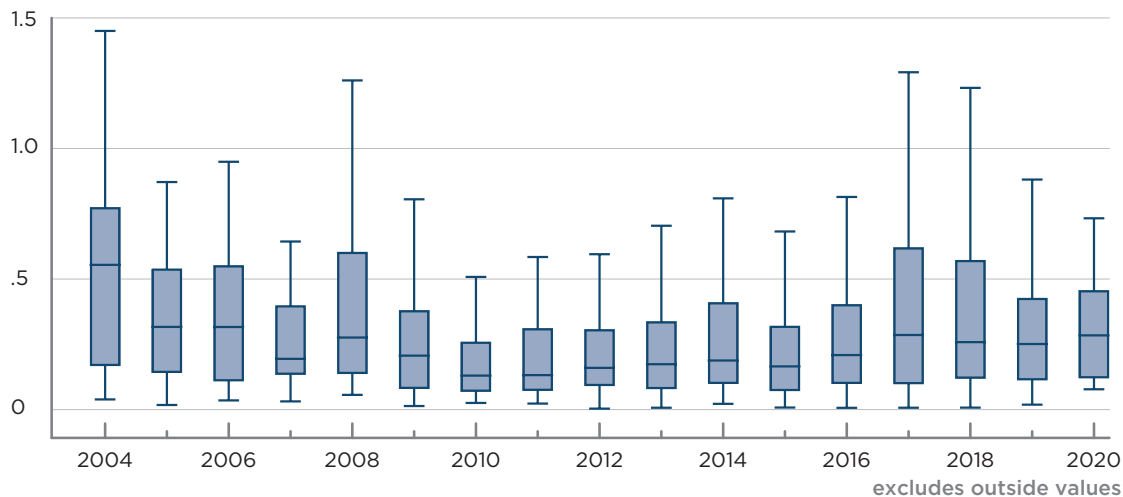
Figure A2

Distribution of civil monetary penalties (CMP) for repeat and/or willful violators, 2005-20**Panel A: Repeat, nonwillful**

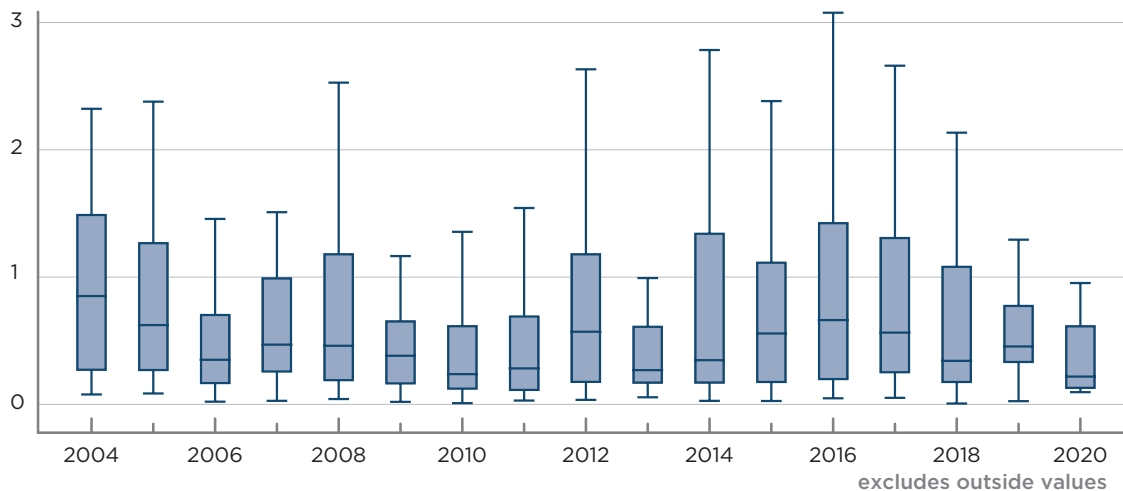
CMP per dollar of back wages

**Panel B: First-time, willful**

CMP per dollar of back wages

**Panel C: Repeat, willful**

CMP per dollar of back wages



Note: "Findings end date" is the latest date in which the Department of Labor found violations, not the year the investigation was concluded.

Source: Department of Labor WHISARD.



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