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## *The Economic Development Benefits of Prevailing Wage* May 2006

The prevailing wage concept stems from a concern that unbridled competition among employers to pay low wages in construction would lead to a less-skilled and less-productive workforce and to shoddy construction practices and unsafe public buildings and infrastructure. The New York State Labor Law (Article 8, section 220) requires that "prevailing wages" and "supplemental benefits" be paid on most public works construction projects. In practice, prevailing wage rates and benefit contributions are usually those established by collective bargaining agreements covering at least 50% of workers in a given area.

Prevailing rates of wages and supplements in New York are determined annually on a county-by-county basis. The New York State Department of Labor is charged under state law with updating and enforcing prevailing wage requirements, except in New York City where the New York City Comptroller has that responsibility. Prevailing wage goes hand-in-hand with the apprenticeship system. As stated in Article 23 of New York's Labor Law, "it is the declared public policy of the state of New York to develop sound apprenticeship training standards and to encourage industry and labor to institute training programs.

In recognition of the value and benefits of rigorous apprenticeship training, prevailing wage regulations permit construction employers to pay registered apprentices wages equivalent to 40% to 50% of journeyman wages. To be paid less than the trade-specific journeyman wage rate on a prevailing wage project, an apprentice must be individually registered in an apprenticeship program that is registered with the state Labor Department. Prevailing wage requirements also set allowable ratios of apprentices to journeymen. For the latest schedule of prevailing wage and benefit rates, see: <http://wpp.labor.state.ny.us/wpp/publicViewPWChanges.do?method=showIt>

### *What is the true cost impact of prevailing wage?*

While opponents of prevailing wage argue that it drives up construction costs, such a view ignores the full range of implications for construction companies, worker training, safety, and the broader impact on economic development.

Arguments against prevailing wage often are rooted in a simplistic view that equates higher wage rates with higher overall construction costs and stops there. This approach misses far more than it comprehends. In reality, considerable research shows that wage standards in general, and prevailing wage regulations in construction in particular, have several economic positive benefits.

- **Costs:** Prevailing wage does not raise overall costs since higher construction wages are usually offset by greater productivity, better technologies, and other employer savings.

- **Skills:** Prevailing wage increases the supply of apprenticeships and worker skills.
- **Worker safety:** Prevailing wage reduces construction injuries and workers compensation costs.
- **Health and pension benefits:** Prevailing wage requirements raise health and pension coverage for construction workers.
- **Cost shifting to taxpayers:** Prevailing wage minimizes the shifting of health coverage and other costs to taxpayers and other employers and workers.
- **Economic opportunity:** Prevailing wage improves wages and economic opportunities for less-educated workers.
- **Curbing harmful competition:** Prevailing wage minimizes a destructive economic “race to the bottom”.
- **Economic development.** Prevailing wage promotes “high-road” local economic development.

### ***Research Findings on the Economic Impact of Prevailing Wage***

The balance of this issues brief summarizes key findings from the labor economics literature on the impact of prevailing wage regulations.

**Costs.** A growing body of economic research concludes that labor standards like prevailing wage do not raise construction costs. First of all, wage and benefit costs are only about one-third of overall construction costs and that share has been falling. As noted above, under prevailing wage, contractors are permitted to pay apprentices in registered programs much less than the prevailing wage for skilled journeymen. More importantly, wage levels are only part of the cost story. Research shows that skilled construction workers who receive higher wages are about 20 percent more productive than less skilled workers. All else being equal, higher productivity means lower unit costs. When workers are better paid, construction companies save because they have less need for supervisors or unskilled labor, and their recruitment and screening costs are less. In addition, higher wages encourage construction companies to use labor-saving technology and more innovative work practices to reduce unit labor costs without reducing wages.<sup>1</sup> Studies of the repeal of state prevailing wage laws have found that the consequences of repeal have included lower quality construction and increased cost overruns.<sup>2</sup>

**Skills.** Construction projects and construction jobs are temporary. Most construction workers change employers when they move from construction project to construction project. In this context, most construction employers have little incentive to invest in worker training. Any investment they might make in skills or apprenticeships is typically lost to them when the construction project ends and the worker moves on to another employer. Economists refer to this as a “market failure” since the normal working of the market leads employers to under-invest in worker skills.<sup>3</sup> Using data for a large number of states from the U.S. Labor Department's Bureau of Apprenticeship and Training, economist

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<sup>1</sup> Steven G. Allen, “Unionized Construction Workers are More Productive,” *The Quarterly Journal of Economics*, vol. 99 (2), May 1984, 251-274; Kevin Duncan and Mark J. Prus, “Prevailing Wage Laws and Construction Costs: Evidence from British Columbia's Skills Development and Fair Wage Policy,” in *The Economics of Prevailing Wage Laws*, edited by Hamid Azari-Rad, Peter Philips, and Mark J. Prus, London: Ashgate Publishing Limited, 2005; Dr. Anthony P. Carnevale, “The Davis-Bacon Act: A Closer Look,” Testimony presented to the U.S. Senate, Labor and Human Resources Committee, Feb. 22, 1995, p. 9.

<sup>2</sup> For example, see Dale Belman and Paula B. Voos, “Prevailing Wage Laws in Construction: The Costs of Repeal to Wisconsin,” Milwaukee: The Institute for Wisconsin's Future, 1995.

<sup>3</sup> Hamid Azari-Rad, “Prevailing Wage Laws and Injury Rates in Construction,” in Azari-Rad, Philips and Prus.

Cihan Bilginsoy found that state prevailing wage laws increase the supply of apprenticeships and that investments in worker training helps apprentices complete their training sooner than in jurisdictions without prevailing wage requirements.<sup>4</sup>

**Worker Safety.** Construction is a dangerous industry. Construction accounts for about 6% of private sector employment but 23% of workplace fatalities and about 10% of non-fatal occupational injuries. Using data from the Bureau of Labor Statistics Survey of Occupational Injuries and Illnesses, SUNY-New Paltz economics professor Hamid Azari-Rad showed that state prevailing wage regulations reduce injuries on construction sites and reduce worker compensation costs. According to Azari-Rad, prevailing wage requirements set in motion a causal chain of higher wages, better training, safer construction work, the retention of experienced workers and an environment where other regulations such as tax laws, insurance coverage and safety rules are followed. Construction companies that compete based on cheapening labor also tend to circumvent workers' compensation coverage, a development that reduces the incentive to create a safe workplace and shifts the costs of workers compensation to other employers.<sup>5</sup>

**Health and Pension Benefits.** The construction industry is characterized by many small employers, the seasonal nature of construction work and the relatively short duration of construction projects. In the absence of collective bargaining, these factors make it less likely that construction employers will provide health and pension benefits. Collective bargaining overcomes this "market failure" feature by establishing multi-employer and jointly managed health and welfare funds that provide health and pension benefits. By establishing wage and benefit standards, prevailing wage requirements take the costs of providing health and pension benefits out of the bidding process and are associated with greater health and pension coverage for construction workers, reducing costs to the public.<sup>6</sup>

**Cost Shifting to Taxpayers and Other Employers.** In the absence of prevailing wage standards or collective bargaining protections, most construction workers in the U.S. do not have employer-provided health insurance. It is well established that the health of the uninsured suffers from delayed medical attention, and that they often receive medical care only in hospital emergency rooms.<sup>7</sup> Unless they pay for their own health insurance (or have coverage through a spouse), construction workers without employer-provided health insurance generally turn to Medicaid or other publicly subsidized health care, or receive care at safety-net hospitals and clinics (uncompensated care). This leads to the costs of health care delivery being shifted from construction companies that do not provide health insurance to taxpayers or to other employers and workers in the form of uncompensated care costs added onto health insurance premiums paid by others. For example, in his study of uncompensated care in the booming Las Vegas area in the late 1990s, economist Jeffrey Waddoups found that a disproportionate share of uncompensated care expenditures resulted from the low incidence of employer-provided health insurance in that area's construction industry.<sup>8</sup> A prominent

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<sup>4</sup> Cihan Bilginsoy, "Wage Regulation and Training: The Impact of State Prevailing Wage Laws on Apprenticeship," in Azari-Rad, Philips and Prus.

<sup>5</sup> Hamid Azari-Rad, "Prevailing Wage Laws and Injury Rates in Construction," in Azari-Rad, Philips and Prus.

<sup>6</sup> See the research summarized in the following chapters in Azari-Rad, Philips and Prus: Jeffrey S. Peterson and Erin M. Godtland, "Benefits vs. Wages: How Prevailing Wage Laws Affect the Mix and Magnitude of Compensation to Construction Workers"; C. Jeffrey Waddoups, "Health Care Subsidies in Construction: Does the Public Sector Subsidize Low Wage Contractors?"; and Mark A. Price, "Pension and Health Insurance Coverage in Construction Labor Markets."

<sup>7</sup> J. Hadley, "Sicker and Poorer: The Consequences of Being Uninsured," report prepared for the Kaiser Commission on Medicaid and the Uninsured, Washington, D.C.: Urban Institute, 2002.

<sup>8</sup> C. Jeffrey Waddoups, "Health Care Subsidies in Construction: Does the Public Sector Subsidize Low Wage Contractors?" in Azari-Rad, Philips and Prus.

national research firm, Data Resources Incorporated, projected that the repeal of prevailing wage in Massachusetts would increase state unemployment compensation and social service expenditures.<sup>9</sup>

**Economic Opportunity.** In testimony before Congress, national education and workforce development expert Anthony P. Carnevale stated, construction “is one of the few remaining sectors where workers with limited classroom education can make a living wage and support a family.”<sup>10</sup> Prevailing wage helps maintain wage standards in the construction industry and thus improves the likelihood that construction jobs will continue to provide an avenue for economic mobility for less educated workers.

**Curbing harmful competition.** Prevailing wage requirements help ensure that competition among contractors in bidding for construction projects is channeled into areas of overall cost efficiency, high productivity and innovative methods, and not unduly focused on driving down wages and benefits. By effectively removing labor standards from competition, prevailing wage works to improve overall industry compliance with wage and hour and safety standards.

**Economic Development.** Prevailing wage exemplifies good economic development. It encourages the development of a high-skill, high-wage economy that provides decent health and pension benefits and economic security to workers. It discourages construction companies from competing based on driving down wages and cheapening the quality of construction, i.e., from a "race to the bottom". Additionally, higher wages have a positive impact on local incomes and tax revenues. In a 1995 study a group of researchers at the University of Utah found that after Utah repealed its prevailing wage law in 1981, construction earnings fell, leading to substantially lower income tax and sales tax revenues.<sup>11</sup> Belman and Voos, economists at the University of Wisconsin, estimated that repeal of that state’s prevailing wage law would significantly reduce construction workers’ incomes and trigger a loss in state tax revenues.<sup>12</sup>

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**Conclusion.** An extensive economics literature shows that prevailing wage in construction means more cost-effective construction, and more skilled and better-paid workers. Industrial development authorities exist to enhance local economic development. Applying prevailing wage requirements to publicly-subsidized construction is likely to lead to a series of benefits that is the flip side of what has happened where prevailing wage has been repealed: higher construction wages, greater health and pension coverage, greater apprenticeship opportunities for less educated workers, and the more effective functioning of the construction labor market overall. Prevailing wage standards are a fundamental building block for a strong local, "high-road" economy based on high skills and high wages.

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<sup>9</sup> Data Resources Incorporated, “Study of the Economic Impact of Repeal of the Massachusetts Prevailing Wage Law,” August 18, 1995, cited in Carnevale, "The Davis-Bacon Act: A Closer Look," Testimony presented to the U.S. Senate, Labor and Human Resources Committee, Feb. 22, 1995, p. 10.

<sup>10</sup> Dr. Anthony P. Carnevale, "The Davis-Bacon Act: A Closer Look," Testimony presented to the U.S. Senate, Labor and Human Resources Committee, Feb. 22, 1995, p. 3.

<sup>11</sup> Peter Philips, Garth Magnum, Norman Waitzman, and Anne Yeagel, “Losing Ground: Lessons from the Repeal of Nine ‘Little Davis-Bacon’ Acts,” University of Utah, 1995.

<sup>12</sup> Dale Belman and Paula B. Voos, “Prevailing Wage Laws in Construction: The Costs of Repeal to Wisconsin,” Milwaukee: The Institute for Wisconsin’s Future, 1995.