

Economic Commentary #40

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# **WEAKENING PREVAILING WAGE HURTS LOCAL CONTRACTORS AND WORKERS**

**A Case Study from Southern Indiana**



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### **Introduction**

A prevailing wage law, also called a common construction wage law, supports blue-collar workers employed in public construction. Prevailing wage is essentially a minimum wage for construction workers. The policy ensures that workers employed on infrastructure projects funded by taxpayer dollars are compensated according to rates normally paid on similar projects in an area.

By ascertaining the local market rate, a prevailing wage law prevents units of government from undercutting wage standards in a community. This ensures that workers can afford to live in the county where they are building a road, school, or other public project. Preventing government from awarding bids to contractors that pay less than the privately-established local market rate also levels the playing field for contractors. The law discourages cut-rate contractors with cheaper, less-trained workers in other states from coming in, getting the work, and taking their earnings and tax dollars home with them upon project completion.

Despite an emerging academic consensus that shows state prevailing wage laws have no discernible impact on project costs but do benefit local contractors, there have been concerted efforts across the country to weaken or repeal these laws. While the majority of U.S. states have a prevailing wage law, at least 11 states have considered weakening their laws over the past three years– including Illinois, Missouri, Wisconsin, Michigan, Indiana, and Kentucky ([Manzo et al., 2016a](#)). A state prevailing wage law can be weakened by limiting the scope of public works covered by the law, changing how prevailing wage rates are determined, or raising the contract threshold– which is the minimum cost of a public project at which point prevailing wage applies.

Indiana provides a recent case study on the effects of weakening prevailing wage on in-state contractors. Indiana’s prevailing wage law – called Common Construction Wage – was changed multiple times from 2012 through 2015. In 2012, projects with an actual construction cost of less than \$250,000 were excluded from coverage under the law. The threshold was subsequently raised on January 1, 2013 to projects costing less than \$350,000. Then, in 2015, lawmakers completely repealed the Indiana Common Construction Wage Act effective July 1 of that year.

This Midwest Economic Policy Institute (MEPI) Economic Commentary explores the effect of weakening Indiana’s prevailing wage law along Indiana’s southern border. The findings of the report can be summarized in three key takeaways:

- Public works construction lost 885 jobs along the state line in Indiana counties but gained 770 jobs in Kentucky border counties after Indiana weakened its prevailing wage law;
- Earnings decreased for construction workers in Indiana counties but increased across the border in Kentucky counties after Indiana weakened its prevailing wage law;
- Weakening Common Construction Wage in Indiana primarily benefited out-of-state contractors at the expense of local businesses and local workers.

## The Cost of Weakening Prevailing Wage Laws

Economic research finds that weakening prevailing wage laws has significant negative economic consequences, particularly for local contractors. Without an effective prevailing wage law, cut-rate contractors with cheaper, less-trained workers in other states can come in, win public bids, and take taxpayer dollars back with them to their own states upon project completion. Data from the 2012 *Economic Census of Construction* reveals that states with weak prevailing wage laws or no law at all have 2.4 percent less of the total value of construction work completed by in-state construction firms compared to states with strong or average prevailing wage laws (Manzo & Bruno, 2016). Similarly, one economist discovered that the probability of winning a bid on a public school construction project is 5 percent lower for out-of-state contractors in states with prevailing wage laws (Prus, 1999). Another study concluded that repealing prevailing wage in San Jose, California would cause 6 percent of the value of public projects to leak out of the county economy to out-of-area businesses (Duncan, 2011).

Recent peer-reviewed analysis finds that weakening prevailing wage in Michigan would eliminate 11,000 total jobs, reduce the state’s gross domestic product by \$1.7 billion, and lower state and local tax revenues by \$28 million (Duncan et al., 2015). The data show that weakening prevailing wage reduces worker wages, particularly for the lowest-paid construction employees. Further analysis concludes that, if all states with strong or average prevailing wage legislation decided to weaken their laws, an additional 102,000 blue-collar construction workers would rely on food stamps, 319,000 would lose health insurance coverage, and the corresponding loss of income tax revenue and increased reliance on public assistance would cost U.S. taxpayers at least \$4 billion per year (Manzo et al., 2016b). Local contractors are hurt, local blue-collar construction workers are pushed into poverty, and tax revenues decline when prevailing wage is weakened.

## Background and Indiana’s Southern Border Prior to Weakening the Law

Prior to Indiana raising its contract threshold to \$350,000, hourly earnings for construction workers in Indiana were similar to all neighboring states except Kentucky (Figure 1). In July 2012, the average construction worker earned \$27.34 an hour as a base wage. Their counterparts across the border in Michigan and Ohio both earned between \$25 and \$26 an hour on average. Construction workers in Illinois, where the cost of living is higher, earned \$34.07 per hour.

**Figure 1: Average Construction Worker Hourly Wage by Midwestern State, July 2012**

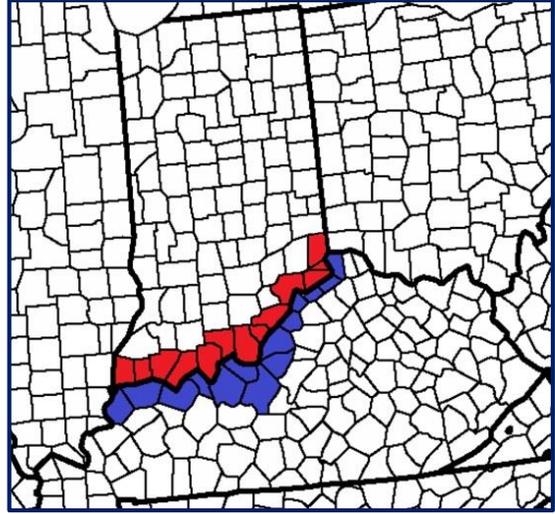
Construction Worker Hourly Wages by State	
State	July 2012
Illinois	\$34.07
Indiana	\$27.34
Kentucky	\$22.08
Michigan	\$25.13
Ohio	\$25.83

Source: BLS, 2016 – “Employment, Hours, and Earnings – State and Metro Area.”

Economic research suggests that lower-paid, out-of-state contractors will flood the public construction market after a prevailing wage law is weakened or repealed. If true, the greatest threat to Indiana contractors would come from across its southern border in Kentucky, where

construction workers earned \$22.08 an hour on average in July 2012 (Figure 1). This was over \$5 less per hour than construction workers earned in Indiana, even though Kentucky has a prevailing wage law.

Indiana's southern border with Kentucky should thus be a good case study on the impact of weakening prevailing wages. Border counties share similar labor force characteristics to one another and are part of the same integrated regional economy (Allegretto et al., 2013). There are 13 Indiana counties that share a border with Kentucky: Clark, Crawford, Dearborn, Floyd, Harrison, Jefferson, Ohio, Perry, Posey, Spencer, Switzerland, Vanderburgh, and Warrick. Similarly, across the way are 14 Kentucky counties: Boone, Breckinridge, Bullitt, Carroll, Daviess, Gallatin, Hancock, Hardin, Henderson, Jefferson, Meade, Oldham, Trimble, and Union.



Data are analyzed for the “heavy and civil engineering construction” sector of the economy from the Quarterly Workforce Indicators (QWI) dataset (Census, 2016). Heavy and civil engineering construction comprises contractors and workers whose primary activity is the construction of entire infrastructure projects. Construction and maintenance of highways, streets, bridges, dams, parks, trails, water lines, sewer lines, oil pipelines, power stations, and plots of land are all included in this section. The vast majority of this work is funded by the public sector using taxpayer dollars.

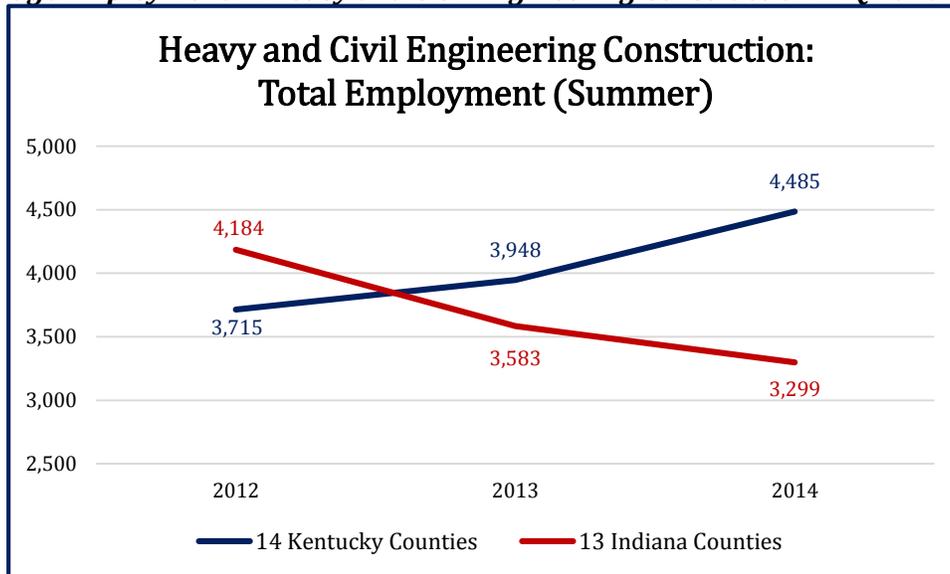
### **Change in the Heavy and Civil Engineering Sector after Weakening the Law**

After weakening prevailing wage, employment in the heavy and civil engineering sector fell in Indiana's southern-most counties but grew across the river in Kentucky border counties (Figure 2). In the second quarter (April through June) and the third quarter (July through September) of 2012, there were 4,184 workers employed in heavy and civil engineering construction in the 13 Indiana counties. Concurrently, there were an average of 3,715 heavy and civil engineering construction workers in the 14 counties across the border. After the Common Construction Wage threshold was raised to \$350,000, southern Indiana's public works construction sector had only 3,299 workers employed during the summer months. This is an employment loss of 885 workers, or 21.2 percent. Meanwhile, public works construction employment increased by 770 workers (20.7 percent) in the Kentucky border counties to 4,485 employees.

In addition, the average monthly earnings of employees in heavy and civil engineering construction careers declined after prevailing wage was weakened in the Indiana counties but increased across the river in the Kentucky counties (Figure 3). After adjusting for inflation, the county-level earnings of public works construction workers averaged \$5,107 per month in the 13 Indiana counties in 2012. Monthly earnings were just \$4,512 on average in the 14 Kentucky counties. Raising the Common Construction Wage threshold to \$350,000 resulted in a wage cut for Hoosier workers. After weakening the law, heavy and civil engineering construction worker earnings fell to \$4,667 per month by 2014, a decline of \$439 per month for the average worker. At

the same time, average monthly earnings increased to \$5,122 for comparable workers across the border in the Kentucky counties, a gain of \$610 every month.

**Figure 2: Average Employment in Heavy and Civil Engineering Construction in Q2 and Q3, 2012-2014**



Source: *Census, 2016* – “LED Extraction Tool – Quarterly Workforce Indicators (QWI).”

These data corroborate previous economic research. In this integrated regional economy along the Ohio River, the evidence suggests that out-of-state contractors from Kentucky with lower-paid construction workers were the real beneficiaries of Indiana weakening its prevailing wage law. Prior to weakening the law, the 14 border counties in Kentucky had fewer workers in heavy and civil engineering construction than the 13 Indiana counties, and the Kentucky workers earned 11.7 percent less per month. Within two years of weakening the law, the Kentucky counties had significantly more workers in the sector than the Indiana counties, and they now earned 9.7 percent more on average every month.

**Figure 3: Average Earnings in Heavy and Civil Engineering Construction in Q2 and Q3, 2012-2014**

Average Monthly Earnings of Employees with Stable Jobs, Adjusted for Inflation (County-Level)		
Year: Quarters	Indiana	Kentucky
2012: Q2 & Q3	\$5,106.52	\$4,511.53
2013: Q2 & Q3	\$4,834.04	\$4,807.16
2014: Q2 & Q3	\$4,667.46	\$5,121.85
Change: 2012-2014	-\$439.06	+\$610.32

Source: *Census, 2016* – “LED Extraction Tool – Quarterly Workforce Indicators (QWI).”

Notwithstanding the actual economic evidence, Indiana lawmakers enacted a full repeal of Common Construction Wage on July 1, 2015. By then, the negative consequences of weakening prevailing wage were apparent to local contractors and local workers in Indiana. In fact, the *South Bend Tribune* reported that “[n]umerous construction company officials testified against the proposal..., saying the law contributes to the state having a stable, well-trained labor force” (*South Bend Tribune, 2015*).

Figure 4 revisits Figure 1 to evaluate the change in hourly earnings for all construction workers across the entire State of Indiana before the threshold was raised from \$250,000 to \$350,000 right

up to the point of full repeal. After Indiana weakened Common Construction Wage, the average hourly earnings of all Hoosier construction workers – on both public and private projects – fell by 2.3 percent, from \$27.34 an hour to \$26.70 an hour. Conversely, construction worker wages increased in all neighboring states. With a wage growth of 11.6 percent over three years, the largest gains for construction workers occurred in Kentucky.

**Figure 4: Change in Average Construction Worker Wage by Midwestern State, July 2012 to July 2015**

<b>Change in Construction Worker Hourly Wages by State, Not Adjusted for Inflation</b>			
<b>State</b>	<b>July 2012</b>	<b>July 2015</b>	<b>Change: 2012-2015</b>
Illinois	\$34.07	\$36.69	+7.69%
Indiana	\$27.34	\$26.70	-2.34%
Kentucky	\$22.08	\$24.63	+11.55%
Michigan	\$25.13	\$25.90	+3.06%
Ohio	\$25.83	\$26.87	+4.03%

Source: BLS, 2016 – “Employment, Hours, and Earnings – State and Metro Area.”

### Conclusions and Implications

The economic data suggests that out-of-state contractors benefited when prevailing wage was weakened. After Indiana weakened Common Construction Wage, higher-paid public works construction workers in the state’s 13 southern-most counties were replaced by lower-paid workers across the border in 14 Kentucky counties. This substantiates previous economic research which finds that weakening prevailing wage hurts local contractors. The redistribution of jobs and earnings to Kentucky construction workers has an adverse impact on income tax revenues and sales tax revenues in Indiana. While post-repeal data is not yet available, these negative outcomes are likely to have been compounded over the past year.

This case study should be a cautionary note to lawmakers in states across the Midwest who are considering weakening their state’s prevailing wage. Prevailing wage is a policy that promotes high-road economic and community development. Weakening prevailing wage only hurts local contractors and workers.

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