Building Up New York, Tearing Down Job Quality

Taxpayer Impact of Worsening Employment Practices in New York City's Construction Industry

A Fiscal Policy Institute Report
www.fiscalpolicy.org

December 5, 2007

Preface

The Fiscal Policy Institute's recent report, *One New York: An Agenda for Shared Prosperity*, outlines policies to help the state's diverse regions and populations grow together and to strengthen and expand the middle class. Enforcing employment standards and leveling the playing field among businesses are key elements of FPI's One New York agenda and should be major public policy priorities in New York City's booming construction industry.

This report lends detail to the vision in One New York and builds on FPI's recent report, *The Underground Economy in the New York City Affordable Housing Construction Industry*, and other research reports on New York's labor market, economic trends, social insurance programs, and the minimum wage. FPI has done a number of other studies dealing with New York's construction industry. In 2004, in conjunction with the Building Trades Employers' Association and the Consortium for Worker Education, FPI published *Building Jobs: A Blueprint for the "New" New York*, a study of the "white collar" or "non-trades" segment of the construction employment market. In April 2006, the New York City Employment and Training Coalition and the New York City Workforce Investment Board published a profile of the New York City construction labor market prepared by FPI. A brief literature survey, "The Economic Development Benefits of Prevailing Wage," was released in May 2006. These and other FPI reports can be found at: www.fiscalpolicy.org.

A closely related FPI report was released in January, 2007, *New York State Workers' Compensation: How Big Is the Coverage Shortfall?* That report demonstrated the need for New York State to undertake a concerted enforcement commitment and strategy to ensure compliance with the state workers' compensation laws. The workers' compensation report also examined the issue of the misclassification of workers as independent contractors by employers seeking to shirk their responsibility for payment of payroll taxes, social insurance premiums and employee fringe benefits.

Comments and questions on this report should be directed to FPI's Deputy Director and Chief Economist, James Parrott, Ph.D., who can be reached at 212-721-5624 or parrott@fiscalpolicy.org.

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Executive summary

The New York City construction industry employs over 200,000 workers—much more than indicated by the official government payroll job numbers. Residential construction activity continues at a high level and together with increased infrastructure and commercial building, the construction sector is soaring to new heights. However, the industry's otherwise bright prospects are marred by worsening wage and employment standards in a large and growing underground segment of the industry.

- As buildings go up in New York City, more and more construction work has gone underground, signifying violation of several employment and tax laws. An estimated 50,000 New York City construction workers—nearly one in four—are either misclassified as independent contractors or employed by construction contractors completely off the books.

- The costs of the illegal underground construction industry to taxpayers are substantial and growing. These fiscal costs were an estimated $489 million in 2005 and are likely to reach at least $557 million in 2008. Contractors in the underground economy skirt payment of legally required payroll taxes and workers compensation premiums and shift these and other costs onto taxpayers and their competitors who play by the rules. Three categories of costs were estimated for 2005:

    - $272 million in unpaid legally mandated payroll taxes for social security and Medicare, and social insurance premiums covering workers' compensation, unemployment insurance and disability insurance.

    - $148 million in health care costs shifted onto the workers themselves, taxpayers and other employers that provide employee health insurance.

    - $70 million in lost personal income taxes because there is no withholding for underground economy workers and/or they are paid off the books.

The underground construction industry is concentrated in residential construction, but also exists in commercial construction, especially in the boroughs outside of Manhattan, and even among some infrastructure projects that are entirely government-funded. While two-thirds of the affordable housing sector is underground, it accounts for only about one-fifth of the entire underground construction sector.

The taxpayer costs quantified above do not include harder-to-quantify economic costs borne by workers and responsible contractors.

- Construction safety reached crisis proportions last year when 29 construction workers were killed on the job in New York City. This necessitated a strong government enforcement response and Occupational Safety and Health Administration (OSHA) reports 22 construction fatalities in 2007. OSHA data indicate a strong correlation between construction fatalities and the characteristics of the underground economy: half of the deaths occurred among workers at very small construction companies, three-fourths of the workers involved worked for non-union companies, and failure to provide safety training was cited in over half of the cases.

- Despite the dangerous working conditions, workers in the underground economy are paid very low wages, are denied the protections of universal social insurance programs (workers' compensation, unemployment insurance, disability), do not have health coverage or retirement benefits, are not able to join a union, and rarely are they entitled to paid sick leave, holidays or vacations. Working in the underground construction economy is like working in the 19th century when it comes to labor rights, protections and employment standards.

- An estimated 43,000 New York City construction workers earn less than $11 an hour, not much above the federal poverty guideline for a family of four.

- Contractors operating in the underground economy also disadvantage law-abiding companies by shifting costs and exploiting workers. Among other things, law-abiding construction contractors pay several hundred dollars per worker to cover medical costs for the employees of underground businesses not providing health coverage.

The underground economy in construction has grown rapidly in recent years as government has failed to effectively enforce employment standards and tax laws. As in the case of environmental pollution, markets on their own do not force businesses to "internalize" all the costs they generate. Over decades, government established a series of employment standards and social insurance systems to protect workers and responsible businesses from unchecked competition that degrades working conditions and the economic well being of workers and that disadvantages responsible businesses.

In particular, state government has failed to act to curb the spread of illegal misclassification of workers as independent contractors. Some businesses do this to skirt employer obligations for payroll taxes, social insurance premiums and other mandated employment costs. In recent years, state government has largely turned a blind eye to this practice that affects an estimated 10 percent of all New York workers, and a much higher percent within construction. In pledging to curb misclassification through tougher enforcement, Governor Spitzer recently characterized the problem as "rampant" and an "epidemic".

Unionization, which could help provide a counter-weight to exploitative employment practices, has declined from 63 percent in the early 1990s to about 45 percent in New York City (calculated as a percentage of all trades workers, including an estimated 50,000 workers misclassified or working off the books). Unfair cost advantages for underground contractors make it increasingly hard for unionized contractors to compete.

The prevailing wage concept was originated decades ago in the construction sector to serve as a check on cut-throat competition among employers based on reducing wages and cheapening working conditions. Unrestrained wage-based competition not only drove down wages but also resulted in a less-skilled and less-productive workforce and a less-safe workplace. This race to the bottom is widespread today in the underground economy with workers squeezed and a host of illegalities involving non-compliance with payment of payroll taxes and non-compliance with social insurance and other essential labor and safety protections. People who do not mind the underground economy are fond of criticizing prevailing wage for allegedly driving up costs. Such a view ignores the full range of implications for construction companies, worker training and well being, safety, and the broader fiscal and economic impacts.

- The underground economy shifts many costs to others while construction companies paying prevailing wage internalize these costs, provide their workers with health insurance and retirement security, and compensate their workers at levels that make possible a middle class living standard.

- Prevailing wage means a more skilled and more productive workforce. Since unit costs are what is important, it is not clear that prevailing wage is more costly when all associated costs are internalized and quality and productivity factors are taken into account.

- And importantly, since prevailing wage carries with it an apprenticeship training requirement, companies paying prevailing wage also fund an extensive program of worker skill and safety training. The result of this mandatory training investment is a highly skilled and more productive workforce and a far safer workplace.

The prevailing wage economy offers workers a career, economic security and a path into the middle class. The underground construction economy offers none of that, and it puts workers at a far greater occupational risk, and cheats workers, taxpayers, law-abiding employers on a large scale.

Recommendations

The spread of the underground economy in New York City's construction industry has worsened employment practices and reduced real wages. It is a problem and a threat not only in construction, but more broadly. It imposes substantial costs on workers, responsible contractors and taxpayers. Government has an obligation to curb the underground economy, enforce long-standing employment laws, ensure compliance with essential social insurance protections and eliminate the unfair competitive advantage from contractors in the underground economy.

- New York City government should work with New York State to vigorously enforce employment laws, ensure compliance with tax laws and social insurance requirements, and use various leverage points to improve pay and working conditions.

- New York City and New York State should require prevailing wage for all affordable housing contracts and for any construction project benefiting from city and state government funding, subsidy or zoning or other land use action. Taxpayers get better value with prevailing wage. It is an effective anti-poverty program, and an obvious way to address New York's widening income gap between the rich and the poor.

- Enforcement efforts should be pursued in a fashion that benefit an often vulnerable workforce that includes many black and Hispanic workers long shut out of opportunities for good-paying jobs, skill development and advancement, or who are recent immigrants.

Introduction

The construction industry and construction workers literally build New York, creating the workplaces, houses, apartments, schools, hospitals, public spaces, transportation arteries, bridges and water tunnels essential to our city's existence, smooth functioning, and quality of life. Construction work is often physically demanding and dangerous, but it offers some of the highest wages available for workers with limited formal education. An extensive apprenticeship system provides many of the industry's workers with the craft skills required for the city's demanding construction projects, skills that can provide secure career ladders and command respectable wages.

Between the city's 12,000 construction companies and over 30,000 self-employed construction workers, the New York City construction sector employs well over 200,000 persons. This is about twice the size of the New York City construction industry’s payroll employment—110,000 in 2005 according to the State Labor Department—the most common yardstick to gauge the magnitude of this industry.

Construction work is project-based, with workers and companies migrating from one job to the next. Most construction companies are trade-specific contractors or employers, such as electrical, plumbing, masonry, or roofing. General contractors serve as organizing agents, working with engineers and architects and coordinating the entire array of trade contractors. Most residential contractors are very small businesses, averaging 4 to 10 employees, while most non-residential contractors are only slightly larger, averaging 15 to 25 employees.

Commercial construction activity dropped sharply in the wake of the recession and downturn early in this decade. And while publicly-funded infrastructure spending continued and residential construction surged, total reported payroll employment in construction declined from mid-2001 through the third quarter of 2004 and only surpassed the previous peak level in mid-year 2007. In October 2007, the official payroll employment count for New York City construction was 126,000 (seasonally adjusted.) The sharp rebound in commercial construction over the past two years and the continued strength in residential construction account for the recent growth in payroll construction jobs.

Reflecting the housing boom sweeping many parts of the country in recent years, the city has seen the biggest surge in residential construction activity since the early 1970s. More housing units were constructed in the past four years than in the entire decade of the 1990s. Despite the nationwide housing slump that began over the past year, local residential construction continues at a high level.

Given several large commercial construction projects (rebuilding at Ground Zero, downtown Brooklyn, new stadiums for the Yankees and the Mets, the Atlantic Yards Arena, and mega-developments over the West Side Rail Yards), major public transportation projects (the Fulton transit hub, the World Trade Center PATH station, the Moynihan train station, the extension of the 7 subway line to the Hudson Yards area) and the City's ambitious 5-year school construction plan, employment is likely to expand considerably over the next five years. Housing construction is also likely to stay reasonably healthy considering the City's commitment to build more affordable housing. There are also several indications that the volume of construction activity related to residential and commercial renovation work will remain high.

The New York Building Congress projects a record $27.5 billion in construction spending in the city in 2008, a one-third increase over 2005. A significant portion of the privately-funded commercial construction in New York City benefits from direct or indirect City and State government subsidy and/or City and State zoning or other land use actions. Government capital spending constitutes the largest segment of the construction market with a projected 2008 value of $12.6 billion. Commercial construction more than doubled between 2005 and 2007 and is forecast to reach $9.5 billion in 2008. The number of residential units constructed in the city nearly doubled between 2002 and 2007, and the value of residential construction is expected to be slightly over $5 billion in 2008.[1]

1. New data on the size of the construction industry

According to the Census Bureau's American Community Survey (ACS)[2], there were 200,000 persons working in the construction industry in New York City in 2005. This includes 155,100 residents of New York City working here, 28,400 persons who reside in the New York suburbs and elsewhere in New York State, and 16,200 people who work in New York City but live in New Jersey, Pennsylvania or Connecticut.[3] See Figure 1 below.

This 200,000 figure is much greater than the 2005 payroll employment level of 110,000 for city construction companies reported by the New York State Department of Labor. The payroll figures do not include the self-employed or the workers who are misclassified as independent contractors or employed "off the books" on a strictly cash basis. The ACS identifies 32,800 persons working in the construction industry in New York City as self-employed. Almost 57,000 other workers who identify themselves as wage and salary workers must, in effect, be "misclassified" (some workers who should be considered "employees" but who are paid as "independent contractors") or workers who are employed off the books.[4]

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[1] New York Building Congress, "New York City Construction Outlook, 2007-2009," prepared by Regina Armstrong, Urbanomics, October 2007.

[2] The American Community Survey (ACS) is conducted annually by the U.S. Census Bureau and is the government's largest annual survey of socioeconomic conditions. Among other data, the ACS provides information on place of work and place of residence, allowing a detailed look at all of the workers engaged in the New York City construction industry.

[3] These figures do not include the 25,000 workers in construction occupations that work outside of the construction industry, e.g., carpenters and electricians working for the public school system or the Metropolitan Transit Authority. See Fiscal Policy Institute, *The New York City Construction Labor Market, A Labor Market Profile Prepared for the NYC Employment and Training Coalition and NYC Workforce Investment Board*, April 2006.

[4] Because of significant growth since 2005, there are probably 225,000 to 240,000 total workers in New York City construction at the end of 2007. It is very likely the estimated number of workers misclassified

While this burgeoning underground economy in construction is heavily populated with immigrant workers, it is not an immigrant problem. It is a problem created by businesses cutting corners at the expense of workers, and by government standing by while that happens.

Persons employed in construction in New York City, 2005

American Community Survey	Employees	Self-employed	Total by area
NYC residents	126,939	28,208	155,147
Residents of NYS outside of NYC	25,434	2,951	28,385
Residents of NJ, PA, or CT	14,621	1,628	16,249
Total by employment status	**166,994**	**32,787**	**199,781**

Estimates by industry segment	Payroll employment	Self-employment	Misclassified workers or employed off the books	Total by segment
Residential construction *	38,500	14,250	29,000	81,750
Non-residential construction	71,500	18,550	28,000	118,050
Total construction **	**110,000**	**32,800**	**57,000**	**199,800**

* Residential construction: payroll employment from Quarterly Census of Employment and Wages, NYS Department of Labor; for other categories see FPI "The Underground Economy in the New York City Affordable Housing Construction Industry," April 17, 2007, Appendix Table 1.
** Total construction: payroll employment from Quarterly Census of Employment and Wages (QCEW), NYS Department of Labor; Total for both segments and self-employment total set equal to ACS 2005 total for persons working in New York City; misclassified and employed off the books estimated as the residual between the ACS and QCEW series.

Figure 1.
Sources: FPI analysis of American Community Survey micro data and New York State Department of Labor Quarterly Census of Employment and Wages employment for 2005.

or working off the books is correspondingly higher at the end of 2007 than in 2005. In addition, the Current Population Survey for the 2004-to-2006 period indicates an even greater gap with the payroll employment data than in the ACS.

2. New York City construction at a critical juncture

The New York City construction industry is at a critical juncture. The volume of construction activity is again rising rapidly, and will reach new heights in the years ahead. Yet, the state of labor practices is very worrisome and there are continuing concerns about widespread safety issues.[5] In the construction industry there has been an increase in employee misclassification, a rash of construction-related occupational fatalities, a decline in unionization, and a decline in real wages for most construction workers.

Increase in employee misclassification

There is considerable evidence that many employers are treating workers as independent contractors when they are actually employees in order to circumvent employer liability for payroll taxes and social insurance premiums. Employee misclassification creates significant problems for workers. Misclassified workers are not covered by workers' compensation, unemployment insurance, or temporary disability insurance. They are liable for the full Social Security and Medicare payroll tax (15.3 percent)[6], and if the payroll tax is not paid, the amount of Social Security benefits for which they are eligible may be reduced. Such workers also lose overtime pay and access to employer-provided health and other benefits, such as retirement benefits and paid time off.

This past August, Governor Spitzer stated: "For years, State government has turned a blind eye on a growing epidemic that is keeping wages and benefits artificially low. The problem is the rampant misclassification of workers."[7] And as Governor Spitzer also noted, misclassified workers lose the right to unionize. In September, the Governor signed an Executive Order establishing a Joint Enforcement Task Force to address the problem of employee misclassification. The Task Force includes the state labor, tax and insurance departments, the State Attorney General and the New York City Comptroller—the City Comptroller has the responsibility under state law for enforcing state prevailing wage requirements within New York City. Upon signing the Executive Order, the Governor stated that it would "protect worker rights while leveling the playing field for law abiding employers so they are not at a competitive disadvantage to employers who refuse to play by the rules as they exploit hard working New Yorkers."[8]

A team of researchers from the Cornell Industrial and Labor Relations School examined unemployment insurance audits to gauge the extent of employee misclassification in New York. Their study estimated that about 705,000 New York workers were misclassified as

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[5] For an extensive narrative account of the growing problem of employment and labor law violations in several industries in New York City, see Annette Bernhardt, Siobhan McGrath and James DeFilippis, *Unregulated Work in the Global City*, New York: Brennan Center for Justice, 2007.
[6] The combined employer and employee payroll tax rates for Social Security and Medicare total 15.3 percent of gross wages.
[7] Governor Eliot Spitzer, "Economic Security in One New York," Speech delivered at the Upper Manhattan Workforce 1 Career Center in New York City, August 13, 2007.
[8] New York State Office of the Governor, "Governor Spitzer Signs Executive Order to Prevent Employee Misclassification," Press Release, September 7, 2007.

independent contractors. For the 2002-to-2005 period of the Cornell study, misclassification affected 10.3 percent of all New York private sector workers. In the construction industry, which was a special focus of the Cornell report, misclassification affected over 45,000 workers, 14.8 percent of all workers.

A study prepared for the U.S. Labor Department stated that employer avoidance of responsibility for workers' compensation premiums was the number one reason employers sought to misclassify workers as independent contractors.[9] In its report on the widespread non-compliance with workers' compensation in New York, FPI underscored the prominent role that misclassification played in workers' compensation fraud.[10]

Considerable evidence suggests that there has been a sharp increase in misclassification in recent years. A recent Illinois study that was similar to the Cornell study in examining unemployment insurance audits, estimated that misclassification affected roughly the same percent of the workforce in Illinois as in New York, and that there had been a 55 percent increase in misclassification from 2001 to 2005.[11]

While the trend in misclassification per se has not been documented for New York, its increase is suggested by rapid growth in two data series that include misclassified workers—the non-employer series and the proprietors' employment series. Workers paid as independent contractors receive an IRS 1099 form for tax purposes rather than a W-2 form at the end of the year. The Census Bureau counts workers paid on 1099 forms as "non-employer establishments." Most people counted as "sole proprietors" are legitimately small businesses. And many people counted as non-employer establishments may indeed be truly consultants or independent contractors. However, the growth in the non-employer and proprietors' employment series has been so much greater than the growth in the payroll employment series that it likely reflects an increase in misclassification.

According to government data, from 2000 to 2005 the absolute number of non-employers in New York grew by 240,500 (20 percent) and the absolute number of proprietors increased by 415,918 (28 percent). Meanwhile, private payroll employment increased by just 33,500 (0.5 percent).[12]

Rise in New York City construction occupational fatalities

Construction safety reached crisis proportions last year when 29 construction workers were killed on the job in New York City. This necessitated a strong government

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[9] Planmatics, Inc. "Independent Contractors: Prevalence and Implications for Unemployment Insurance Programs," Prepared for the U.S. Department of Labor, Employment and Training Administration, February 2000, p. iii.

[10] Fiscal Policy Institute, *New York State Workers' Compensation: How Big Is the Coverage Shortfall?* January 25, 2007.

[11] Michael P. Kelsay, James I. Sturgeon, and Kelly D. Pinkham, "The Economic Costs of Employee Misclassification in the State of Illinois," A report by the Department of Economics, University of Missouri-Kansas City, December 6, 2006.

[12] See FPI, *The State of Working New York, 2007,* Figure 2.10, p. 22.

enforcement response. In the most recent federal fiscal year through September 30, 2007, there were 22 construction fatalities, according to the Occupational Health and Safety Administration (OSHA). OSHA data indicate a strong correlation between construction fatalities and the characteristics of the underground economy: half of the deaths in 2007 were among workers at very small construction companies, three-fourths of the workers involved worked for non-union companies, and failure to provide safety training was cited in over half of the cases.[13] (See Figure 2.)

Many of the construction fatalities in 2006 were connected to the lack of training in the use of scaffolds on construction sites. In November of 2006, Mayor Bloomberg established a task force on construction scaffold safety. The task force's report found extensive noncompliance with safety and health and Buildings Department regulations, noting that few workers were aware of existing safety and training requirements. The task force recommended the establishment of a Scaffold Enforcement Unit within the City's Buildings Department.[14] Over the past year, the City's Buildings Department has added 67 inspector positions and launched new initiatives to address scaffold safety and other enforcement problems.[15]

Decline in construction unionization

As in the case of pollution, there is "market failure" in that markets themselves do not force construction contractors to internalize all of the costs they generate. Where markets fail, government needs to step in. But until very recently, there was little government enforcement against illegal employment practices in the New York City construction industry.[16] In a market economy, unions can be an effective counterweight to illegal employment practices. However, the extent of unionization in the industry has fallen considerably compared to 15 years ago.

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[13] Richard Mendelson, Area Director, Manhattan Area Office, OSHA, "2007 Construction Safety Report Card," BTEA Safety Conference, November 20, 2007. Of the 29 construction fatalities in 2006, OSHA reported that two-thirds of the construction workers killed on the job worked for very small contractors and that 86 percent occurred on the job sites of non-union employers. Richard Mendelson, Area Director, OSHA Manhattan, "2006 New York City Construction Safety Report Card," Presentation at BTEA Safety Conference, November 21, 2006.

[14] Mayor Bloomberg's Scaffold Task Force Report, "Steps to Safety: Recommendations for Improving the Safety of Workers on Suspended Scaffolds," December 2006. The Task Force Report was released on February 2, 2007.

[15] Commissioner Patricia J. Lancaster and First Deputy Commissioner of Operations Robert LiMandri, "Building a Safer NYC," NYC Department of Buildings, November 20, 2007.

[16] For a discussion of labor standards enforcement efforts, see Fiscal Policy Institute, *The Underground Economy in the New York City Affordable Housing Construction Industry*, April 17, 2007, pp. 16-17. When Governor Spitzer signed his Executive Order to prevent employee misclassification, State Labor Commissioner Patricia Smith noted that the Joint Enforcement Task Force would "reverse several years of lax enforcement." Governor Spitzer Press Release, September 7, 2007.

Construction workers killed in New York City, 2002-2007

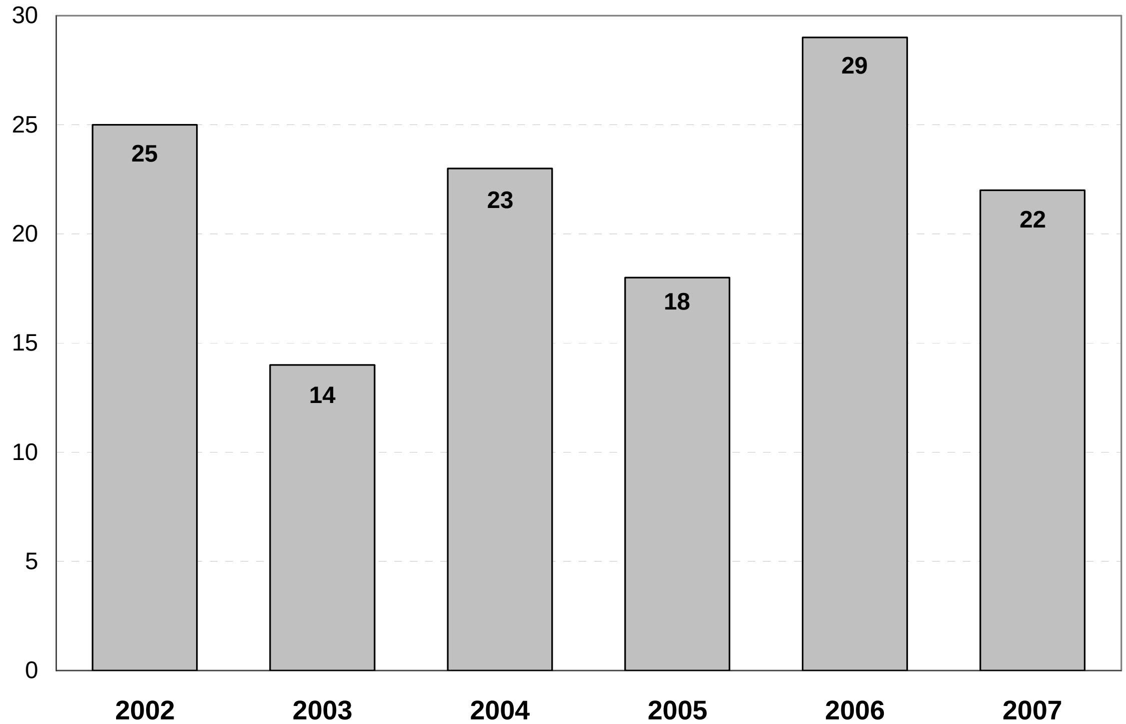

Figure 2.
Source: Occupational Safety and Health Administration.

Union density is measured as the number of union members as a percentage of the estimated total number of construction trades workers in New York City. The denominator *excludes* the self-employed and the non-trades portion of the industry (i.e., managerial, professional and administrative workers), but it *includes* the 50,000 misclassified as independent contractors and those working off the books. While the number of unionized construction trades workers increased from 66,000 in the early 1990s to 76,000 for the 2004-to-2006 period, the number of non-union workers has more than doubled since the early 1990s. From a union density of 63 percent in the early 1990s, FPI estimates that New York City's construction unionization fell to 45 percent in the 2004-to-2006 period. (See Figure 3.)

Unionization among New York City construction trades workers

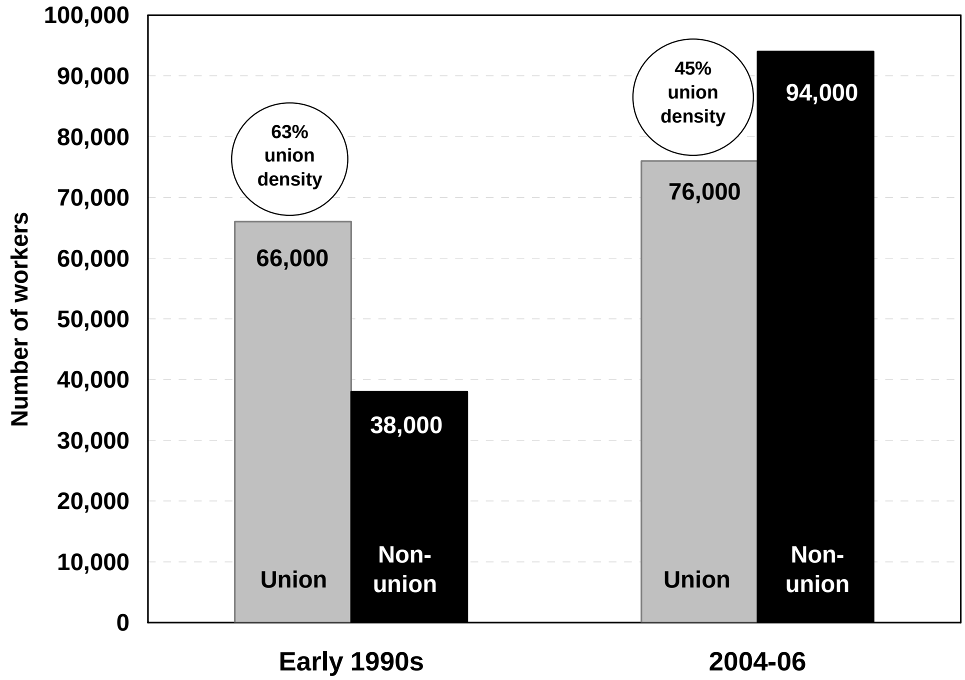

Figure 3.
Source: FPI estimates based on 1990-2006 CPS and 2005 ACS. Non-union total for 2004-06 includes several thousand misclassified independent contractors and workers employed off the books. Estimates are for trades workers in the New York City construction industry.

The decline in unionization means that real wages are likely to decline further, that less skill and safety training will take place, and that likely will be less of a check on the erosion of labor conditions.

Decline in real, inflation-adjusted construction wages

The substantial extent of underground employment practices in the construction industry makes it difficult to reliably gauge wage trends. The two most readily available data sources indicate somewhat different trends.

The wage data compiled by the New York State Department of Labor in connection with the administration of the unemployment insurance system provides a look at the trend in average wages by industry for payroll jobs located in New York City. This data, referred to as insured employment, represents the workers on the books and properly classified, and include non-trades managerial, professional and administrative workers (it excludes workers in the underground economy). According to the insured employment data, shown in Figure 4, the average inflation-adjusted construction wage in 2006 was only slightly above the 1990 level. Driven heavily by large wage increases for the best-paid wage and salary workers on Wall Street and in high-end professional and information services, the average real wage in New York City rose by one-third between 1990 and 2006. In construction, however, the average wage increased by just 1.5 percent over this period. From 2003 to 2006, Figure 4 shows a sharp divergence in the annual wage trends between construction workers and the average across all industries; for all workers the inflation-adjusted wage grew by 8.8 percent from 2003 to 2006, while the average construction worker saw a 4.9 percent decline.

Average annual wages, in constant $2006, all industries and construction, New York City, 1990-2006

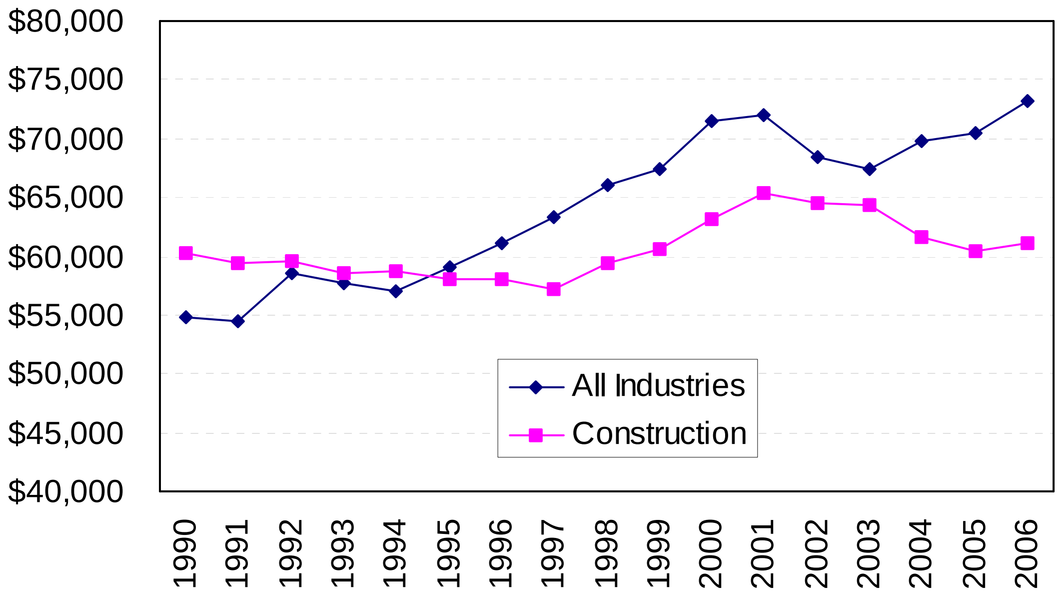

Figure 4.
Source: New York State Department of Labor, Quarterly Census of Employment and Wages.

The Census Bureaus' Current Population Survey (CPS) provides a look at hourly wages for all workers and paints a far bleaker picture. Because of sample size limitations in the CPS that limit analysis of wage trends to city residents, it is not possible to include commuters working in New York City.[17] Using a trendline technique to gauge the change in the inflation-adjusted median construction industry hourly wage for city residents indicates a 19 percent decline between 1990 and 2006. This is shown in Figure 5. For unionized city residents working in the construction industry, the median real wage fell

[17] The American Community Survey provides data on wage and salary earnings over the prior 12 months for both city residents and commuters, but the ACS microdata needed to do this first became available for 2005.

by 12 percent over this period. For non-unionized resident workers, who have a median hourly wage of $14 compared to about $20 for unionized resident workers, the real median wage dropped by five percent. The greater decline among union workers might reflect the movement to the suburbs of some more highly-paid union construction workers and the increase in lower-paid apprentices in recent years as the volume of construction activity has grown. The fact that the number of lower-paid, non-union workers has grown so rapidly since 1990 (Figure 3) explains how the all-worker wage decline could be so much more (19 percent) than either the union wage decline (12 percent) or the non-union wage decline (5 percent).

Real median hourly wage, NYC resident wage and salary construction workers, 1990-2006

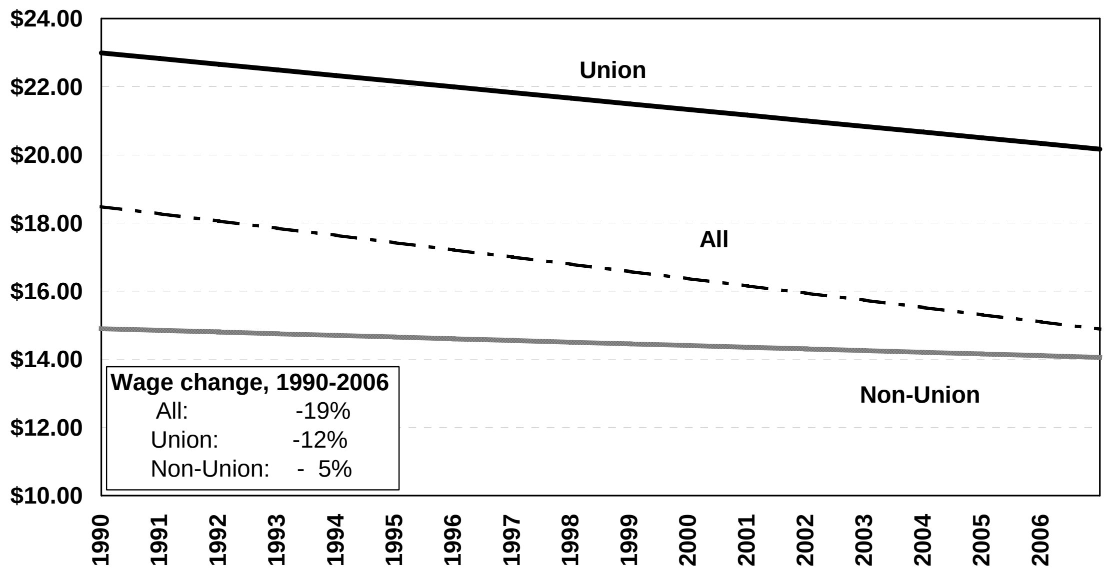

Figure 5.
Source: FPI analysis of Current Population Survey data. Includes non-trades workers. Median hourly wages in constant, $2006, deflated using New York metro CPI. Includes non-trades workers and underground workers; excludes self-employed.

3. The fiscal implications of worsening employment practices

Employee misclassification and off-the-books activity not only drive down the wages of workers but also lead to several other adverse fiscal and economic effects. Employers who misclassify workers or employ workers off the books may shave their costs but only at the expense of government which loses tax revenue and sees increased demands made on various government programs, and at the expense of other employers who operate within legal requirements regarding payroll taxes and social insurance protections. These illegal activities also contribute to wage and income inequality through generalized pressure on the wages of less-educated workers. Employers engaging in misclassification and off-the-books activity do not really save costs; they just shift them onto workers, other businesses, government and society at large.

From the point of view of labor protections and wage levels, there is not a huge difference between employers who misclassify workers as independent contractors and those who employ workers off the books. Both types of employers are breaking the law, and neither makes payroll tax payments or social insurance premium payments on behalf of such workers. In New York State, private employers are required to provide coverage for all three social insurance programs (workers' compensation, unemployment insurance, and disability insurance). Generally, employers who do not make payroll tax or social insurance premium payments deprive workers of coverage under these programs. Since Social Security and Medicare are general safety net programs, most workers will be eligible for at least minimum benefits, regardless of the payroll taxes paid in on their behalf. Workers injured on the job can qualify for workers' compensation benefits even if their employer has not made premium payments on their behalf. Such workers are paid out of a special fund financed through an assessment on premiums paid by employers providing regular workers' compensation coverage. In any case, there is a fiscal cost, or revenue loss, to government that results from employers not making payroll tax or social insurance premium payments, and a shifting of responsibility from underground contactors to responsible contractors.

There is also likely to be cost shifting involving health care costs that results from employers who illegally employ workers. Since the affected workers will not have employer-provided health insurance, the workers are left to fend for themselves. Given their low wages, such workers likely would qualify for Medicaid coverage; however, many will not avail themselves of that. If they cannot qualify for Medicaid, and they are injured on the job or otherwise require medical assistance, emergency rooms will provide uncompensated health care services. Medicaid and uncompensated care both involve the shifting of costs from employers illegally employing workers to taxpayers and employers providing health coverage to their employees.

This section of the report develops estimates of the fiscal impacts of the underground economy in New York City's construction industry. Five steps are involved in estimating the fiscal impacts. First, an estimate of the number of workers engaged in the trades segment of the New York City construction industry is developed, including a distribution for five categories of wage and tax compliance status. Second, per worker payroll taxes and social insurance premiums are calculated for workers at the different hourly wage levels used in this analysis. Third, industry-wide estimates are made of the payroll taxes and social insurance premiums lost due to employer noncompliance with applicable employment laws. Fourth, since most of the workers involved in this industry do not have employer-provided health insurance, estimates are made of the health care costs shifted to Medicaid and other payers. Fifth and finally, the amount of personal income tax liability is estimated for workers at different hourly wage levels and estimates are made of the lost personal income taxes for a portion of workers who are assumed to be noncompliant in paying income taxes.

Figure 6 shows the estimated number of trades workers in the New York City construction industry and the distribution of workers by employment and tax status. These estimates are based on FPI's examination of several government data sources. Fiscal estimates are made for workers at various wage levels applicable to the New York City construction industry (Appendix Figure 1 explains the basis for these wage levels).

NYC construction trades workforce, by category of worker

Category of worker	Share of trades workforce	Number of workers	Hourly wage *
Union worker	45.5%	61,800	$33.00
Non-union employee	17.7%	24,000	$15.00
Misclassified independent contractor, paying own payroll taxes	12.3%	16,667	$12.00
Misclassified independent contractor, not paying payroll taxes	12.3%	16,667	$11.00
Off-the-books worker	12.3%	16,667	$10.00
Total, all workers	**100%**	**135,800**	

Note: This figure includes construction trades workers only; excluded are non-trades (managers, professionals and administrative workers) and self-employed. Misclassified workers and off-the-books workers are not union.
* Hourly wage rates are detailed in the notes to Appendix Figure 1.

Figure 6.
Source: Estimates by Fiscal Policy Institute.

For each category of worker, Figure 7 shows the total annual amount of payroll taxes and social insurance premiums that should be, but is not, paid, given the wage rate involved. Workers' compensation premiums represent the single largest component. (Appendix Figure 1 shows the individual components for each wage category.) According to the New York Compensation Insurance Rating Board, the workers' compensation premium rate, including assessments, is $14.67 dollars per $100 dollars of payroll in residential construction. For example, at a wage level of $10 an hour, an employer should be paying a workers' compensation premium of $2,699 per year. At the $33.00 an hour union rate, the workers' compensation premium totals $8,351. Including all payroll tax and social insurance premium payments yields a total of $6,007 for a $10 an hour construction worker, ranging up to $17,553 annually for the typical union construction worker.

There is another big difference besides the fact that one number is nearly three times the other: while the union contractor is paying nearly $18,000 per worker, many non-union contractors working underground are paying nothing.

Lost payroll taxes and social insurance premiums from the underground NYC construction industry

		Lost payroll taxes and social insurance premiums, versus employers paying all payroll taxes and social insurance	
Trades workers only Category	**Number of workers**	**Per worker amount ***	**Total (dollars in millions)**
Union worker	61,800	$0.00	$0.0
Non-union employee	24,000	$0.00	$0.0
Misclassified independent contractor, paying own payroll taxes	16,667	$3,731.42	$62.2
Misclassified independent contractor, not paying payroll taxes	16,667	$6,558.22	$109.3
Off-the-books worker	16,667	$6,006.77	$100.1
Total, all trades workers	**135,800**		**$271.6**

* See Appendix Figure 1 for details.

Figure 7.
Source: Estimates by Fiscal Policy Institute.

Figure 7 uses the per worker payroll tax and social insurance premium data from Figure 6 to estimate the public costs in lost payroll taxes and lost social insurance premium payments. At current wage rates, lost payroll taxes and social insurance premium payments for misclassified independent contractors and off-the-books workers total $271.6 million per year.

The public often bears the cost of providing health coverage to the non-union construction workforce. Generally, in New York City's construction industry, only unionized workers have employer-provided health insurance.[18] U.S. Labor Department data indicate that the construction industry in New York City has a much higher than average incidence of occupational injuries than other industries. In 2004, male construction workers accounted for 13.9 percent of occupational injuries and illnesses suffered by male New York City private sector workers, nearly four times the construction share of NYC private employment (3.7 percent). In 2005, construction accounted for 28 percent of fatal occupational injuries among New York City males.[19]

Figure 8 provides estimates of the health care costs shifted to other payors by construction employers not providing health insurance. For the roughly 74,000 New York City construction workers without employer health insurance, it is assumed that one-fourth receives coverage under Medicaid, and a slightly lower portion, one-fifth, receive uncompensated health care services.[20] Thus, the estimated cost to taxpayers of providing Medicaid coverage to roughly 18,500 construction workers is $111 million annually, and the cost of providing uncompensated health care services to 14,800 workers is $37 million annually. The total in $148 million annually in shifted health care costs.

[18] A recent United Hospital Fund report that provides the most detailed data on health insurance coverage in New York does not provide data on coverage by industry for New York City. In New York State, 33.9 percent of construction workers were uninsured in 2003-2004. This is the highest for the nine industry groupings presented. Very few New York City adults with incomes below 200 percent of the federal poverty line have employer-provided health insurance: 39 percent are uninsured and 33 percent have Medicaid. United Hospital Fund, "Health Insurance Coverage in New York, 2003-2004," November 2006.

[19] U.S. Department of Labor, Bureau of Labor Statistics.

[20] Medicaid costs per non-elderly adult average $6,000 annually in New York City. The cost of uncompensated health care services provided affordable housing construction workers was estimated by FPI at $2,500 per worker receiving uncompensated care. Articles consulted in developing this estimate include: Randall R. Bovbjerg, et.al., "Caring for the Uninsured in New York," Urban Institute, October 2006, and C. Jeffrey Waddoups, "Employer Sponsored Health Insurance and Uncompensated Care: An Updated Study of the University Medical Center in Clark County (Las Vegas)," July 2001.

Health care costs shifted to Medicaid and other payers by underground NYC construction contractors

Category of worker	Number of workers	Public cost of Medicaid coverage for 1/4 of workers without health insurance (a)	Cost of uncompensated health care shifted to other payors for 1/5 of workers without health insurance (b)
Union worker	61,800	$0.0	$0.0
Non-union employee	24,000	$36.0	$12.0
Misclassified independent contractor, paying own payroll taxes	16,667	$25.0	$8.3
Misclassified independent contractor, not paying payroll taxes	16,667	$25.0	$8.3
Off-the-books worker	16,667	$25.0	$8.3
Total, all construction trades workers	**135,800**	$111.0	$37.0

Notes: Dollars in millions.
(a) Assumes that a quarter of workers without employer-provided health insurance sign up for Medicaid and that the annual cost of Medicaid-covered health care they receive is $6,000.
(b) Assumes a fifth of workers without employer-provided health insurance receive health care services that fall into the "uncompensated care" category. In New York, the costs for uncompensated care are borne by health care providers (hospitals and clinics) and, through the Health Care Reform Act's uncompensated care surcharge, by employers that provide health insurance to their workers. Given the high incidence of construction accidents, this cost was estimated at $2,500 per worker receiving uncompensated care.

Figure 8.
Source: Estimates by Fiscal Policy Institute.

Under New York State's Health Care Reform Act (HCRA), employers providing health insurance to their employees, such as union construction employers, are mandated to pay a surcharge on certain medical expenses to help cover the cost of uncompensated health care, including the health care for employees of employers not providing health insurance. Thus, under this perverse state provision, responsible employers providing health insurance to their employees, in effect, pay several hundred dollars per worker to cover medical costs for the employees of their competitors who do not provide health coverage.

The high incidence of illegal employment practices in construction also suggests the likelihood of lost personal income tax payments. Workers paid on a cash basis, off the books, are unlikely to pay personal income taxes and many workers misclassified as independent contractors probably fail to report all of their earnings. Only workers officially on a business's payroll records have federal, state and local income taxes withheld from their pay. Figure 9 presents estimates of the additional personal income taxes that would be paid, or owed, by construction workers if all were legally employed on a payroll employment basis and were, thereby, subject to withholding. The estimates in Figure 9 assume that all workers currently subject to withholding pay income taxes and that one half of the workers misclassified as independent contractors pay income tax.[21]

Given current wages rates, lost income taxes are estimated at almost $70 million, with $26 million of that representing New York state and city income taxes.

Lost income taxes due to the underground NYC construction industry

	Lost income taxes vs. workers paying income taxes at current wage rates (dollars in millions)
Federal income tax	$43.5
New York State income tax	$15.2
New York City income tax	$11.0
Subtotal, New York income taxes	$26.2
Grand total, all income taxes	$69.7

Note: These estimates do not include business income tax payments.

Figure 9.
Source: Estimates by Fiscal Policy Institute.

Figure 10 summarizes the three sets of fiscal costs presented in Figures 7, 8 and 9. The total fiscal costs equal an estimated $489 million. This is an estimate based on 2005 employment levels.

The ***fiscal costs*** estimated here do not include the ***economic costs*** borne by the workers themselves. These include abysmally low wages for the dangerous work performed, not being covered by social insurance protections (social security, Medicare, workers' compensation, unemployment or disability insurance), not having pension coverage or family health insurance, no paid time off, and not having the right to join a union.

[21] The personal income tax calculations assume full-year New York City residency and are based on city, state and income tax liability for a single worker with no dependents.

Total fiscal costs of underground NYC construction industry

	Dollars in millions
Lost payroll taxes and social insurance premiums	$271.6
Health care costs shifted to other payors	$148.0
Lost income tax collections	$69.7
Grand total: lost payroll taxes, social insurance premiums, personal income taxes, and health costs shifted to others	$489.3

Figure 10.
Source: Estimates by Fiscal Policy Institute, see Figures 7, 8 and 9.

According to the CPS wage data for the past three years, roughly 45,000 New York City resident construction workers make less than $11 an hour. This wage level roughly translates into the hourly equivalent of the federal poverty guideline for a four-person family.

Contractors operating in the underground economy also disadvantage law-abiding companies by shifting costs and exploiting workers. Among other things, law-abiding construction contractors pay several hundred dollars per worker to cover medical costs for the employees of underground businesses not providing health coverage.

4. The advantages of prevailing wage and why standards matter

The prevailing wage concept stems from a concern that unchecked 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. New York State Labor Law requires that “prevailing wages” and “supplemental benefits” be paid on most public works construction projects. In practice, prevailing wage rates and benefit contributions, by craft, are usually those established by collective bargaining agreements covering at least 50 percent of on the books trades workers in a given area.

Prevailing wage goes hand-in-hand with the apprenticeship system. New York’s Labor Law states: “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 percent to 50 percent of journeyperson wages.

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

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 is falling. While contractors are permitted to pay apprentices in registered programs much less than the prevailing wage for skilled journeypersons, wage levels are only part of the cost story. Research shows that skilled construction workers are 20 percent more productive than less skilled workers. 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 recruitment costs are less. In addition, higher wages encourage companies to use labor-saving technology and more innovative work practices to reduce unit labor costs without reducing wages.[22] 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.[23]

Skills. Most construction workers change employers when they move from construction project to construction project. In this context, construction employers have little incentive to invest in worker training. Economists refer to this as a “market failure” since the normal working of the market leads employers to under-invest in worker skills.[24] Using data for a large number of states from the U.S. Labor Department's Bureau of Apprenticeship and Training, economist Cihan Bilginsoy found that state prevailing wage laws increase the supply of apprenticeships and worker skills.[25]

Worker safety. Construction is a dangerous industry. Nationally, construction accounts for about six percent of private sector employment but 23 percent of workplace fatalities and about 10 percent of non-fatal occupational injuries. As noted earlier, there were a

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[22] Steven G. Allen, “Unionized Construction Workers are More Productive,” *The Quarterly Journal of Economics*, May 1984; Kevin Duncan and Mark J. Prus, “Prevailing Wage Laws and Construction Costs,”, in *The Economics of Prevailing Wage Laws* (EPWL), 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.

[23] 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.

[24] Hamid Azari-Rad, “Prevailing Wage Laws and Injury Rates in Construction,” EPWL.

[25] Cihan Bilginsoy, “Wage Regulation and Training: The Impact of State Prevailing Wage Laws on Apprenticeship,” EPWL.

staggering 29 construction-related occupational fatalities in New York City in 2006. Research shows that state prevailing wage regulations reduce injuries on construction sites and reduce worker compensation costs. 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 cheat the workers' compensation system and other contractors, shifting the costs of workers' compensation to other employers.[26]

Health and pension benefits. Construction is characterized by many small employers, seasonal work and short duration 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 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.[27]

Cost shifting to taxpayers and other employers. 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 uncompensated care at safety-net hospitals and clinics. This shifts health care costs from construction companies not providing health insurance to taxpayers or to other employers in the form of uncompensated care costs borne by employers who do provide health insurance. In his study of uncompensated care in Las Vegas 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 construction.[28] A prominent national research firm, Data Resources Incorporated, projected that the repeal of prevailing wage in Massachusetts would increase state unemployment compensation and social service expenditures.[29]

Economic opportunity. In Congressional testimony, national education and workforce development expert Anthony 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.”[30] Prevailing wage helps maintain wage standards and improves the likelihood that construction 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

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[26] Hamid Azari-Rad, “Prevailing Wage Laws and Injury Rates in Construction,” EPWL.
[27] See the research summarized in the chapters in EPWL by Peterson and Godtland; Waddoups; and Price.
[28] C. Jeffrey Waddoups, “Health Care Subsidies in Construction: Does the Public Sector Subsidize Low Wage Contractors?” EPWL.
[29] Data Resources Incorporated, “Study of the Economic Impact of Repeal of the Massachusetts Prevailing Wage Law,” August 18, 1995, cited in Carnevale, 1995.
[30] Carnevale, 1995.

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 entering or engaging in a race to the bottom. Additionally, higher wages have a positive impact on local incomes and tax revenues. Researchers found that after Utah repealed its prevailing wage law, construction earnings fell, leading to substantially lower income tax and sales tax revenues.[31] 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.[32]

An extensive economics literature shows that prevailing wage in construction means more cost-effective construction and more skilled and better-paid workers. Prevailing wage is good for construction employers and workers and makes good economic sense overall because it fosters 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.

[31] 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.
[32] Belman and Voos, 1995.

The Cast-in-Place-Reinforced Concrete Industry—A New York Success Story

Concrete is an essential historic and modern building material. In addition to its extensive use in highways, bridges, subways and other infrastructure projects, concrete is often used in high-rise building construction. In fact, construction companies and skilled trades workers in New York City have long been industry leaders in developing the techniques now used around the world in structural reinforced concrete construction.

Cast-in-place-reinforced concrete has long been preferred for residential high-rise buildings because of its strength, sound insulation, fire protection, and low maintenance. One of the leaders in affordable housing construction, Artimus Construction, recently completed a 12-story mid-rise residential/mixed-use building in Harlem. Escalating steel prices; the ready, local availability of materials and the skilled labor needed for cast-in-place reinforced concrete; and the speed with which concrete buildings can be constructed were among the factors leading Artimus to build with concrete. Innovative construction techniques pioneered by the local Metallic Lathers Union, such as "post-tensioning," permit wider floor spans, allowing Artimus to economize on the number of columns and create more expansive room layouts.

The Turner Construction Company used cast-in-place-reinforced concrete in erecting the Frank Gehry-designed InterActiveCorporation headquarters across from Chelsea Piers on 11th Avenue in Manhattan. Concrete construction lent itself to the engineering challenges in creating irregular-shaped floor plates and the eight huge glass arcs designed by Gehry to resemble sails on a boat.

The Concrete Alliance includes several skilled trade unions and the Cement League, an organization of union concrete contractors. In addition to the Metallic Lathers Union, the workers who shape and erect reinforcing bar structures, union Carpenters build forms that mold poured concrete, Teamsters drive the trucks delivering ready-mix concrete, Operating Engineers operate the cranes that hoist concrete to upper floors, Cement and Concrete Workers pour concrete, and Cement Masons finish concrete surfaces.

In addition to its various advantages from a design and cost perspective, cast-in-place concrete construction builds the local economy and economizes on transportation costs because it relies to a much greater extent on locally-supplied skills and materials. In high-rise building construction, concrete and steel are often substitutes. However, steel is not produced within the region and is increasingly imported from Asia. The New York City ready-mix concrete industry is a branch of the manufacturing sector, with about 30 companies and 600 high-wage workers. This is in addition to the several thousand skilled trades workers within the construction industry who build with concrete.

Conclusion and recommendations

The New York City construction industry is much larger than usually recognized by regional economists, employing over 200,000 workers. The three main segments of the construction sector—residential, commercial and infrastructure—have grown significantly in recent years and are expected to continue to have strong growth at least over the next three to four years. In a period when the national economy is slowing and could enter a period of weakness, the New York City construction sector promises further growth.

However, the industry's bright prospects are marred by deteriorating employment practices. An estimated 50,000 construction workers in New York City either as misclassified independent contractors or completely off the books. These estimates are informed by the best available government data and extensive discussions with industry insiders.

A host of negative results flow from these deteriorating employment practices. Construction accidents resulting in a growing number of deaths have increased and necessitated a strong response from government. Despite the dangerous working conditions in this industry, wage levels are extremely low, particularly by standards for the construction industry. An estimated 43,000 construction workers are paid less than $11 an hour. Wages for on-the-books construction workers declined about 5 percent, after adjusting for inflation, from 2003 to 2006. Another government data source that includes underground economy workers indicates a 19 decline in inflation-adjusted wages for New York City construction workers since 1990.

Beyond the steep decline in real wages, misclassified and off-the-books construction workers are consigned to a secondary tier of the labor market with limited opportunities to acquire new skills or to move up a career ladder. Very few workers in this industry have health benefits and, given the estimates in this report, 50,000 workers are not covered by workers' compensation, unemployment insurance or state-mandated disability insurance. These workers do not have payroll taxes paid on their behalf by their employers, and employers are not withholding income taxes from wages paid. Many contractors may be completely out of compliance with the various labor standards requirements that have existed in New York State for decades.

Just because the wages are low does not mean that costs are low. Contractors pay construction workers low wages and shift substantial economic costs onto workers and shift considerable fiscal costs to other construction employers and taxpayers generally. These costs may not be reflected in the price of the contract or the cost of a housing unit or a building, but they are certainly real and borne somewhere in the economy. Workers bear the brunt of these costs through low wages, hazardous working conditions and the lack of social insurance or fringe benefits. But there are also costs that push up workers' compensation premiums for other employers, health care costs are shifted to taxpayers or businesses that provide their employees with health insurance, and tax collections are less because these contractors are evading legal requirements.

This report has estimated that the total fiscal costs associated with the employment of several thousand workers as misclassified independent contractors or off the books were $489 million in 2005. Given the growth in the industry since 2005, and the projected growth in the coming year, ***it is likely that these fiscal costs will reach, conservatively, $557 million in 2008.***

Recommendations

The spread of the underground economy in New York City's construction industry has worsened employment practices and reduced real wages. It is a problem and a threat not only in construction, but more broadly. It imposes substantial costs on workers, responsible contractors and taxpayers. Government has an obligation to curb the underground economy, enforce long-standing employment laws, ensure compliance with essential social insurance protections and eliminate the unfair competitive advantage from contractors in the underground economy.

City government is largely responsible for the affordable housing industry that has grown rapidly in recent years and accounts for about 20 percent of the underground construction industry. The City has moved aggressively to address hazardous scaffold safety problems in construction. The logical next step is to recognize and begin addressing pervasive non-compliant labor practices. With the passage of several anti-fraud enforcement provisions in the historic workers' compensation reform legislation signed into law in mid-March, the State is also poised to dramatically improve labor standards enforcement.

- New York City government should work with the State to vigorously enforce employment laws, ensure compliance with tax laws and social insurance requirements, and use various leverage points to improve pay and working conditions.

- The City and the State should require prevailing wage for all affordable housing contracts and for any construction project benefiting from city and state government funding, subsidy or zoning or other land use action. Taxpayers get better value with prevailing wage. It is an effective anti-poverty program, and an obvious way to address New York's widening income gap between the rich and the poor.

- Enforcement efforts should be pursued in a fashion that benefit an often vulnerable workforce that includes many black and Hispanic workers long shut out of opportunities for good-paying jobs, skill development and advancement, or who are recent immigrants.

Appendix

Per worker payroll taxes and social insurance premiums,
NYC construction trades sector

				Misclassified independent contractors		
		Union worker (a)	**Non-union construction employee** (b)	**Paying own payroll taxes** (c)	**Not paying own payroll taxes** (d)	**Off-the-books worker** (e)
Hourly wage		$33.00	$15.00	$12.00	$11.00	$10.00
Hours per year		1,725	1,840	1,840	1,840	1,840
Annual wages		**$56,925**	**$27,600**	**$22,080**	**$20,240**	**$18,400**
	payroll rate					
FICA (f)	0.1240	$7,058.70	$3,422.40	$2,737.92	$2,509.76	$2,281.60
Medicare (f)	0.0290	$1,650.83	$800.40	$640.32	$586.96	$533.60
Unemployment insurance (g)	0.0480	$408.00	$408.00	$408.00	$408.00	$408.00
Federal unemployment tax (h)	0.0080	$56.00	$56.00	$56.00	$56.00	$56.00
Disability (i)	0.0016	$28.29	$28.29	$28.29	$28.29	$28.29
Workers' compensation (j)	0.1467	$8,350.90	$4,048.92	$3,239.14	$2,969.21	$2,699.28
Annual payroll taxes and social insurance premiums if employers comply with NYS law (k)		**$17,552.71**	**$8,764.01**	**$7,109.66**	**$6,558.22**	**$6,006.77**
Annual payroll taxes if paid by misclassified independent contractor				**$3,378.24**		

Notes:
(a) Mean annual wages from NYS DOL Occupational Employment Statistics for New York City construction trades in 2005 (2nd quarter) divided by 1725 annual hours. Since some union contracts have a 35-hour week, union workers on average work fewer total hours per year than non-union workers.
(b) Median non-union hourly wage in construction, 2006, Current Population Survey (CPS), FPI analysis.

(c) Hourly wage at $12.00 is between the 25th percentile ($10.00) and the median hourly wage for non-union workers ($15.00) in the CPS.
(d) Hourly rate of $11.00 is the level below which are 25 percent of New York City construction workers according to the CPS.
(e) Hourly rate of $10.00 is the 25th percentile hourly wage for non-union construction industry workers in the CPS.
(f) Payroll rates for FICA and Medicare are evenly shared between employer and employee, except in the case of a misclassified independent contractor.
(g) According to the NYS Department of Labor, the average unemployment premium rate for New York City residential construction employers in 2006 was 4.8%. Unemployment insurance premiums are paid only on first $8500 of annual wages.
(h) Federal unempopyment tax is paid only on the first $7000 of annual wages.
(i) Under the NY State Insurance Fund, disability premiums for men are 16 cents per $100 of wages and are payable up to a maximum annual wage of $17,680.
(j) According to the New York Compensation Insurance Rating Board, the workers' compensation premium rate, including assessments, in residential construction is $14.67 per $100 of wages.
(k) This calculation is before application of federal or NYS prevailing wage requirements, if applicable.

Appendix Figure 1.
Source: Estimates by Fiscal Policy Institute.

FPI

Fiscal Policy Institute

The Fiscal Policy Institute is a nonpartisan research and education organization that focuses on tax, budget, and economic issues that affect the quality of life and the economic well being of New York State residents.

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