



# OUTSOURCING POVERTY

## Federal contracting pushes down wages and benefits

BY KATHRYN EDWARDS AND KAI FILION

Federal agencies have been under pressure to reduce the size of their workforce and cut costs, creating the incentive to outsource government work through contracts with private businesses for goods and services. Between 2000 and 2006, federal contract spending increased 69.1%—from \$256 billion to \$415 billion.<sup>1</sup> This upsurge in spending represents a growing share of the federal budget: by 2006, the cost of contracting out for goods and services constituted 16.1% of all federal outlays, up from 12.4% in 2000.<sup>2</sup>

In terms of jobs, between 2000 and 2006, the number of federal contract workers increased from 1.4 million to 2.0 million.<sup>3</sup> This compares to 2.7 million federal employees.<sup>4</sup> In short, 43% of all employees who do the government's work are actually employed by *private* businesses.

This Issue Brief examines the wage and benefit standards in government and contracted work. We find that contracted employees are much less likely to earn wages high enough to allow a single full-time worker to put a family of four over the poverty threshold (\$9.91/hour in 2006).<sup>5</sup> We estimate that in 2006, nearly 20% of contracted employees earned wages under this benchmark, while fewer than 8% of federal employees did.

Further, given that federal employees are more likely than those in the private sector to have access to employer-sponsored health insurance or retirement plans, contracting out work almost surely decreases benefit coverage and pays lower wages for many workers.

The outsourcing of government work through federal contracts is often done in the name of cost-saving. However, much of this saving does not come from greater efficiency in provision, but from the willingness and ability of private contractors to push down wages and benefits for employees.

### Wages and benefits for private sector and federal employees

On average, federal workers have higher wages and better fringe benefits than their private sector counterparts, including federal workers at the lower end of the pay scale. Our primary measure of this is the share of workers who

**TABLE 1**

**Federal and private sector workers earning less than \$9.91 an hour (2006)**

	Federal employees	Private sector employees
<i>Number of workers</i>	2,713,000	102,603,032
<i>Number of workers earning below poverty threshold wage</i>	209,650	25,902,619
<i>Share of workers earning below poverty threshold wage</i>	7.7%	25.2%

SOURCE: EPI analysis of Current Population Survey and Current Employment Statistics.

earned below the poverty threshold wage. This paper examines this benchmark for the federal government, the private sector, and federal contract workers.

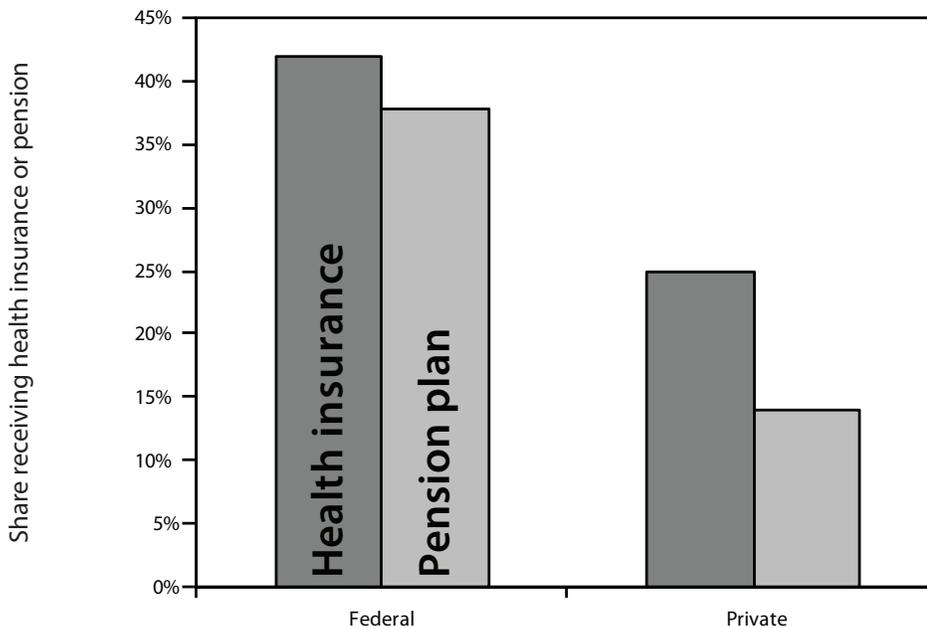
The poverty threshold wage is the hourly earnings a full-time worker would need in order to support a family of four above the poverty line. In 2006, the poverty threshold wage was \$9.91. As **Table 1** shows, only 7.7% of federal employees earned less than \$9.91

in 2006, compared to 25.2% for private sector employees. That is a stark difference; the private sector is three times as likely to employ workers with poverty-threshold wages.

Furthermore, federal employees who do earn less than the poverty threshold wage are much more likely than private sector employees to have employer-sponsored health insurance or retirement plans.<sup>6</sup> **Figure A** shows

**FIGURE A**

**Employer-sponsored benefits for workers earning less than \$9.91 an hour (2006)**



SOURCE: EPI analysis of Current Population Survey and Current Employment Statistics.

that among U.S. workers earning below the poverty threshold wage of \$9.91 per hour, federal employees were far more likely to have employer-provided benefits than private-sector employees. In 2006, 42% of low-wage federal employees had full or partial health coverage and 38% had a retirement plan. This contrasts sharply with private-sector low-wage workers. Only 25% had full or partial health coverage, and 14% had a retirement plan.

Given the significant disparity in pay and benefits between federal and private sector jobs, it is useful to look at the composition of the labor force in each

respective sector to get a demographic snapshot of workers below the poverty threshold.

**Table 2** breaks down federal and private sector employees by gender and race who earned less than \$9.91 an hour in 2006. For both federal and private-sectors, females and minorities are over-represented among workers below the poverty threshold.

### Federal contract workers

The federal government does not collect data on federal contract workers. This study uses data from the

**TABLE 2**

### Characteristics of workers (2006)

	Federal workers		Private-sector workers	
	<i>Number</i>	<i>Share</i>	<i>Number</i>	<i>Share</i>
<b>Total</b>	2,713,000	100.0%	102,603,032	100.0%
<b>Male</b>	1,519,280	56.0%	55,444,903	54.0%
<b>Female</b>	1,193,720	44.0	47,158,128	46.0
<b>White</b>	1,861,118	68.6%	69,370,365	67.6%
<b>Black</b>	461,210	17.0	10,942,215	10.7
<b>Hispanic</b>	198,049	7.3	15,789,159	15.4
<b>Other</b>	192,623	7.1	6,501,293	6.3
<b>Poverty threshold</b>				
<b>Total</b>	209,650	7.7%	25,902,619	25.2%
<b>Male</b>	91,031	43.4%	11,122,078	42.9%
<b>Female</b>	118,619	56.6	14,780,542	57.1
<b>White</b>	108,282	51.6%	14,678,976	56.7%
<b>Black</b>	55,972	26.7	3,592,348	13.9
<b>Hispanic</b>	27,536	13.1	6,138,530	23.7
<b>Other</b>	17,860	8.5	1,492,764	5.8

**SOURCE:** EPI analysis of Current Population Survey and Current Employment Statistics.

General Services Administration and the Bureau of Labor Statistics to estimate the number of contract workers earning below the poverty threshold wage. (The details of this estimation are available in the Methodology Appendix.)

Using data from fiscal year 2006, we estimate that over 406,000 federal contract workers earned less than \$9.91 an hour. This number represents nearly 20% of all federal contract workers in the United States (**Table 3**).

This share of workers earning less than the poverty threshold wage is more than *double* the share among federal employees. Based on the composition of the private-sector workforce that earns below poverty threshold wages, we can safely assume that these workers are disproportionately minority, female, and unlikely to have employer-provided health coverage or pension plans.

The federal government is spending more than it ever has to contract out its work to private industry. Some tout this as a cost-saving and efficient practice, but it comes with a direct cost: decreased wages and benefits for workers who are shunted into lower-paying jobs not protected by internal government employment standards. The result is two federal workforces, one to whom the government is accountable, and one to whom it is not.

## Policy prescriptions

The problem of depressed wages and benefits for federal contract workers is completely solvable. There are already policies in place that serve as a model of how to address this type of problem.

Starting in 2004, the Small Business Administration (SBA) set goals for small business participation in federal

contracts. It encouraged agencies to award contracts to companies owned by women, veterans, and minorities or those located in economically challenged areas and gave them benchmarks to work toward. The targets are specific: 23% of contracts to small business, 5% to woman-owned small businesses, and 3% to disabled veteran-owned and HUBZone small businesses.<sup>7</sup> Every year the SBA produces the Small Business Goaling Report that measures its progress in meeting these goals.

These efforts to support small businesses are an important precedent for putting explicit performance targets in federal contracts. Not only do they recognize that there are flaws in the current system of awarding contracts, but they mandate specific remedies to correct them. The same can and should be done for the wages and benefits of federal contract workers. There are two ways to do this:

1. Require preferential treatment for companies whose workers engaged on the federal contract project are paid above poverty threshold wages and have employer-provided benefits, such as health insurance and a retirement plan.
2. Incorporate wage stipulations into all federal contracts, requiring that any worker engaged on the federal project be paid above the poverty threshold wage—and have strict penalties for firms that fail to do so.

Policies geared to redressing these wage and benefit failures of federal contracts will need monitoring, and should be accompanied by an annual report that assesses the efficacy of worker-protection efforts on an agency-by-agency basis (like the Small Business Goaling Report

**TABLE 3**

### Federal contract workers, 2006

<i>Federal contract workers</i>	2,074,687
<i>Number of workers earning below poverty threshold wage</i>	406,354
<i>Share of workers earning below poverty threshold wage</i>	19.60%

**SOURCE:** EPI analysis of Federal Procurement Data System and Current Population Survey.

---

mentioned above). This would enable the government to identify which agencies are most delinquent. Moreover, a report would require that the federal government begin collecting data on federal contract workers, which it has thus far neglected to do. Better information could lead to more targeted and effective policy.

## **Conclusion**

Federal spending on private contracts totaled over \$400 billion in 2006 and employed a workforce of 2.0 million people. Despite its size, this workforce is often overlooked and unrepresented. In 2006, one in five

federal contract workers was paid less than a poverty threshold wage. While the percent of contract workers earning below poverty threshold wages is lower than in the private sector as a whole, it is more than double the number in the federal workforce and indicates that contracting out has a depressing effect on the incomes and labor standards of people who do work for the U.S. government. The government needs to change the way contracts are awarded to protect these workers, so that taxpayer funds are not used to create an ever larger workforce that is unable to escape poverty and support a decent standard of living.

## Methodology Appendix

The federal government does not collect data on the number of federal contract workers, who these workers are, or their compensation. In order to discover the characteristics of these workers, we looked at private sector workers in the industries in which the federal government spent money. Forty-three percent of workers providing goods to or performing services for the federal government are from the private sector.

To estimate the number of low-wage workers covered by federal contracts, we combined data from the General Services Administration (GSA) on federal contracts with data from the Current Population Survey (CPS) on low-wage workers. Using the dollar value of the contract, we were able to estimate the number of workers employed and then the proportion of those workers that were low wage.

Contract data came from the Federal Procurement Data System Next Generation (FPDS-NG) FY2006 Federal Procurement Report. Each year, the FPDS-NG offers a breakdown in Federal Contract Actions and Dollars, divided by Executive Department, Agency, state, or North American Industry Classification System (NAICS) code in the Federal Procurement Report. This means that we have data on the dollar amount of each action, the location of the work performed, the contracting agency, and the industry in which it was spent. In 2006, this included 3,680,355 actions totaling \$415,003,495,868, and 641,791 over \$25,000.<sup>8</sup>

To estimate the number of jobs on each contract, we matched the dollars spent by NAICS code in the FPDS-NG to the nominal dollar-based Domestic Employment Requirements Matrix for 2006. The output was the number of jobs created in each industry from federal contract spending.<sup>9</sup>

With the number of jobs created allocated to BLS industries, we used data from the Current Population Survey-ORG to estimate how many of those jobs were below the poverty threshold wage. The poverty threshold wage is the amount a full-time worker would have to earn to stay above the federal poverty threshold for a family of four. In 2006, this was \$9.91 an hour. In order to get a large sample size, we took five (2003-07) years of CPS data to determine the proportion of workers that earn below the poverty threshold wage in each in-

dustry. In other words, we found the number of workers in each industry that earned under the poverty threshold wage of that year for five years (\$9.04 in 2003, \$9.28 in 2004, \$9.60 in 2005, \$9.91 in 2006, \$10.19 in 2007). With five years of proportions, we found the average for each industry.

For example, if an industry created two jobs for every million dollars of sales and received \$50 million in federal contracts, that translated to 100 jobs. We then multiplied that jobs number by the share of workers who earned below the poverty threshold in that industry. One hundred jobs in an industry with 6% poverty share would equal six poverty threshold jobs. This was done for each industry to get a total number of jobs created and total number of low-wage jobs created.<sup>10</sup>

This methodology assumes that the same proportion of contract workers earn poverty level wages as workers in the private sector.

A total of 2 million federal contract workers is a very conservative estimate for two reasons. First, the total amount of money spent on procurement by the federal government was \$415 billion. However, the government report only categorizes \$326 billion by industry code. That means that our figure does not account for \$89 billion, a fifth of total contract spending, which could generate an additional 540,000 jobs.

Second, the Employment Requirements Matrix shows the aggregate effect of spending money in an industry. Investing \$100 million into manufacturing creates more than just manufacturing jobs, it creates jobs in janitorial services, trucking companies, financial services, and many other industries and occupations. The matrix generates this residual job creation to show the total effect in each industry, not just the direct recipient of spending. For this report, we looked only at the jobs created in the industry in which the money was spent, an important distinction from looking at jobs in the aggregate because this assumes that there is no spillover effect from contract spending, no subcontracting, and job uniformity within the industry. This eliminates an additional 1.3 million jobs from the analysis, but makes no significant difference in the estimated share of below poverty threshold jobs created.

---

## Endnote

1. Spending was adjusted for inflation using the Consumer Price Index for All Urban Consumers Research Series (CPI-URS).
2. Budget of the United States Government, Fiscal Years 2000 and 2006, Office of Management and Budget.
3. The federal government does not collect data on federal contract workers. This number is an estimate using the General Services Administration's Federal Procurement Data System and the Employment Requirements Matrix from the Bureau of Labor Statistics. For more, see the Methodological Appendix.
4. Employment, Hours, and Earning survey from the Current Employment Statistics of BLS, includes federal postal workers.
5. The Federal Poverty Threshold is determined yearly by the U.S. Census Bureau Housing and Household Economic Statistics Division.
6. By "pension plan" we mean any employer-sponsored retirement plan, including a 401(k) plan where the employer's only contribution is a match of employee contributions, if any. Full-time federal employees, by contrast, are covered by both a defined-benefit pension plan and the Thrift Savings Plan, a 401(k)-like defined-contribution plan. Thus, the comparison understates the difference in benefits between federal employees and the contract workforce.
7. The HUBzone Empowerment Contracting program provides federal contracting opportunities for qualified small businesses located in distressed areas. The program encourages economic development in historically underutilized business zones— "HUBZones"— through the establishment of preferences. <http://www.sba.gov/hubzone/section05b.htm>
8. Federal Procurement Report FY 2006, Section 1, Total Federal Views.
9. The FPDS-NG spending report was given in NAICS codes. The employment requirements matrix is in BLS codes. We used the standard crosswalk between them. Where there were composite codes (i.e., three BLS sectors comprise one NAICS code, or vice versa) we used BLS industry output to weight the dollar division between them.
10. Federal contract spending on public administration, or roughly 4.125% of total spending, does not have a BLS-NAICS crosswalk. In order to include it into job numbers, we found the average number of jobs created per dollar spent and then multiplied that by the public administration spending to get a job creation number. All of these jobs were assumed to be above the poverty threshold wage.