HB 1210

Department of Legislative Services

Maryland General Assembly
2017 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1210 (Delegate Frick)
Economic Matters

Procurement - Prevailing Wage Rates - Applicability to Sheet Metal Fabricators

This bill requires contractors and subcontractors on eligible public work contracts to pay prevailing wages to sheet metal fabricator apprentices and workers employed by a contractor or subcontractor at their place of business if the sheet metal fabricator is performing custom sheet metal fabrication related to the construction of a public work.

The bill applies only prospectively and may not be applied or interpreted to have any effect on any procurement contract entered into or any invitation for bids or request for proposals issued before the bill's October 1, 2017 effective date.

Fiscal Summary

State Effect: General fund expenditures by the Department of Labor, Licensing, and Regulation (DLLR) increase by $48,800 in FY 2018 to enforce the bill. Out-year expenditures reflect annualization and ongoing operating expenses. The cost of prevailing wage projects that use sheet metal fabricators may increase slightly to the extent that prevailing wages for that work exceed current wages paid. Given that sheet metal fabrication usually represents a relatively small component of overall project costs, the effect on total project cost is expected to be negligible. The application of existing penalty provisions for violations of the prevailing wage statute is not expected to have a meaningful effect on revenues.

(in dollars)	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
Revenues	$0	$0	$0	$0	$0
GF Expenditure	48,800	60,500	63,500	66,600	69,900
Net Effect	($48,800)	($60,500)	($63,500)	($66,600)	($69,900)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate increase; (-) = indeterminate decrease

Local Effect: The cost of local public work projects that use sheet metal fabricators may increase slightly for the same reasons as the State. Given that sheet metal fabrication usually represents a relatively small component of overall project costs, the effect on total project cost is expected to be negligible. No effect on local revenues.

Small Business Effect: Potential meaningful for sheet metal fabricators. These firms may experience an operational burden in complying with the requirements of the prevailing wage statute; any increase in labor costs likely is passed on to the State or local governments that pay for the contract.

Analysis

Current Law: For a complete description of the State's prevailing wage statute, please see the **Appendix – Maryland's Prevailing Wage Law**.

Background: DLLR advises that many public work projects involve heating, ventilation, and air-conditioning (HVAC) related work, which often involves sheet metal work to custom design and build ductwork for the HVAC systems. It has determined that, since 2012, 171 individual sheet metal contractors have participated on eligible public work contracts.

State Fiscal Effect: There are two major components to DLLR's enforcement of the prevailing wage statute. First, contractors and subcontractors submit their payroll electronically to DLLR, which is then reviewed by wage and hour investigators. Second, the investigators visit job sites to ensure that work is being performed by the individuals listed on the payrolls and to interview workers at the site.

The bill results in a modest expansion in the number of payrolls reviewed by DLLR and also expands the number of site visits that must be conducted. As most sheet metal fabrication occurs off-site, the number of job sites visited by investigators grows modestly. DLLR's Prevailing Wage Unit is already strained due to recent growth in the number of prevailing wage projects subject to enforcement, and it cannot absorb any additional workload. Therefore, general fund expenditures by DLLR increase by $48,812 in fiscal 2018, which accounts for the bill's October 1, 2017 effective date. This estimate reflects the cost of hiring one wage and hour investigator to enforce compliance with the bill. It includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Position	1.0
Salary and Fringe Benefits	$43,703
One-time Start-up and Ongoing Operating Expenses	5,109
Total FY 2018 State Expenditures	**$48,812**

Future year expenditures reflect a full salary with annual increases and employee turnover and ongoing operating expenses.

The bill does not require any upgrade to DLLR's tracking system or online payroll submission system; sheet metal fabricators can be treated much like any other new contractor that has not previously worked on a prevailing wage project. Similarly, sheet metal fabricator apprentices and workers must be added as a new category to DLLR's survey of contractors and unions to establish regional prevailing wages for those occupations. That can also be done with existing resources.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): University System of Maryland; Public School Construction Program; Department of Labor, Licensing, and Regulation; Maryland Department of Transportation; Department of Legislative Services

Fiscal Note History: First Reader - March 13, 2017
fn/ljm

Analysis by: Michael C. Rubenstein

Direct Inquiries to:
(410) 946-5510
(301) 970-5510

Appendix – Maryland's Prevailing Wage Law

Contractors and subcontractors working on eligible public works projects in Maryland must pay their employees the prevailing wage rate. "Public works" are structures or works, including a bridge, building, ditch, road, alley, waterwork, or sewage disposal plant, that are constructed for public use or benefit or paid for entirely or in part by public money.

Eligible public works projects are:

- those carried out by the State;
- an elementary or secondary school for which at least 25% of the money used for construction is State money; and
- any other public work for which at least 50% of the money used for construction is State money.

Any public works contract valued at less than $500,000 is not required to pay prevailing wages. The State prevailing wage rate also does not apply to (1) any part of a public works contract funded with federal funds for which the contractor must pay the prevailing wage rate determined by the federal government or (2) specified construction projects carried out by public service companies under order of the Public Service Commission.

Prevailing wages are wages paid to at least 50% of workers in a given locality who perform the same or similar work on projects that resemble the proposed public works project. If fewer than 50% of workers in a job category earn the same wage, the prevailing wage is the rate paid to at least 40% of those workers. If fewer than 40% receive the same wage rate, the prevailing wage is calculated using a weighted average of local pay rates. The State Commissioner of Labor and Industry is responsible for determining prevailing wages for each public works project and job category based on annual surveys of contractors and subcontractors working on both public works and private construction projects.

The commissioner has the authority to enforce contractors' compliance with the prevailing wage law. Contractors found to have violated the prevailing wage law must pay restitution to the employees and liquidated damages to the public body in the amount of $20 a day for each laborer who is paid less than the prevailing wage, or $250 per laborer per day if the employer knew or reasonably should have known of the obligation to pay the prevailing wage. If an employer fails to comply with an order by the commissioner to pay restitution, either the commissioner or an employee may sue the employer to recover the difference between the prevailing wage and paid wage. The court may order the employer to pay double or triple damages if it finds that the employer withheld wages or fringe benefits willfully and knowingly or with deliberate ignorance or reckless disregard for the law.

The Governor must include at least $385,000 in the budget each year for the Prevailing Wage Unit within the Department of Labor, Licensing, and Regulation (DLLR).

The University System of Maryland, Morgan State University, St. Mary's College of Maryland, and the Maryland Stadium Authority are all exempt from the prevailing wage law.

History of the Prevailing Wage

The federal Davis-Bacon Act, originally enacted in 1931, requires contractors working on federal public works contracts valued at more than $2,000 to pay their employees the prevailing local wage for their labor class, as determined by the U.S. Secretary of Labor. The general intent of the law, and similar state and local laws, is to stabilize local wage rates by preventing unfair bidding practices and wage competition. Thirty-two states and the District of Columbia currently have prevailing wage laws; since 1979, nine states have repealed their prevailing wage laws.

Maryland adopted a prevailing wage law in 1945 (Chapter 999), but it only applied to road projects in Allegany, Garrett, and Washington counties. In 1969, the statute was amended to include State public works contracts of $500,000 or more. There have been periodic changes to the law and the definition of "prevailing wage." In 1983, the law was broadened to include public works projects in which the State funds 50% or more of the total project costs and 75% or more in the case of public schools. Chapter 208 of 2000 reduced the prevailing wage threshold for public schools from 75% to 50% of construction costs, thereby bringing school construction projects in line with prevailing wage requirements for other public works projects. Chapters 281 and 282 of 2014 further lowered the State funding threshold for school construction projects to 25% of total construction costs, making almost all public school construction projects in the State required to pay the prevailing wage, subject to the $500,000 contract value threshold.

The number of prevailing wage projects has risen dramatically in recent years. DLLR advises that its prevailing wage unit currently monitors about 2,300 projects compared with 187 in fiscal 2011 and 446 in fiscal 2012. To accommodate the increase in projects, the number of prevailing wage investigators increased in fiscal 2016 from three to six, with each having a caseload of about 250 projects at any given time; there are currently five filled positions.

Five Maryland jurisdictions – Allegany, Charles, Montgomery, and Prince George's counties and Baltimore City – have local prevailing wage laws requiring public works projects in the jurisdiction to pay prevailing wages; Montgomery County's prevailing wage ordinance does not apply to school construction projects.

Research on the Effects of Prevailing Wage on Contract Costs

The Department of Legislative Services (DLS) regularly reviews research on the effect of prevailing wage laws on the cost of public works contracts and has found inconsistent and/or unreliable results. The primary challenge confronted by all prevailing wage researchers is identifying an appropriate "control group" consisting of projects of similar type, timing, and location that do not pay the prevailing wage. In most jurisdictions that require a prevailing wage, all projects of a specified type and size are subject to it, so there is no natural control group. Some researchers have compared project costs in states or localities before and after they adopted prevailing wage requirements, but their findings are clouded by the difference in time, during which construction costs changed and other factors were not consistent. Another deficiency in the research is that it almost always relies on project bid prices (*i.e.*, the anticipated cost prior to the beginning of construction) rather than actual final costs. As most construction projects experience change orders or cost overruns affecting their cost, reliance on bid prices negatively affects the validity of the findings. Therefore, research findings related to the effect of the prevailing wage on project costs are inconsistent and often inconclusive. A similar review of research conducted by DLLR for the Task Force to Study the Applicability of the Maryland Prevailing Wage Law also concluded that "data limitations create difficulty for researchers on both sides of the issue."

Early theoretical studies concluded that higher wages under prevailing wage contracts increase contract costs by between 10% and 30%, but many of those studies were flawed, and their findings could not be replicated. For instance, a frequently cited study of 18 projects by the then U.S. General Accounting Office was found to have omitted from its analysis 12 projects in which the prevailing wage was actually lower than the market wage. Empirical studies carried out in the 1990s found much smaller contract cost effects, often in the range of between 2% and 10%, but those studies were hampered by the control group and data quality challenges identified above.

More recent empirical data from several counties yields similar results. Local school systems occasionally solicit side-by-side bids with and without prevailing wages to help them decide whether they want to accept the full State match (and, thus, be subject to the prevailing wage) or a lesser State match without being subject to the prevailing wage. Data provided to the Public School Construction Program by Anne Arundel, Carroll, Frederick, Howard, and Washington counties from 2012-2015 shows that the cost differential between bids with and without prevailing wages for 266 individual bids submitted for 26 different school construction and renovation projects averaged 11.7%, with a range from 0% to 49%. As with other research data, these represent bid prices, not actual construction costs.

These empirical findings have been countered over the past 10 to 15 years by multiple large-scale studies that have found no statistically significant effect of prevailing wages on contract costs. As with the earlier studies that found a project cost effect, control group and data quality issues may have also affected these studies' findings, but the studies themselves cited the following possible explanations for the absence of a cost effect:

- higher wages are associated with higher productivity, reducing the overall cost of the project;
- contractors may be saving money in other areas, such as using lower cost supplies and materials; and
- contractors may absorb some of the cost of paying higher prevailing wages in order to remain competitive in government procurement.

One area of the research in which there is a general consensus, and which is supported by the federal Bureau of Labor Statistics, is that labor costs represent between 20% and 30% of construction costs. Therefore, a 10% gap between prevailing wages and market wages could theoretically increase total contract costs by about 2.5%, and a 40% gap in wages could increase total contract costs by about 10%. That is consistent with the findings of some of the empirical studies that have been conducted, but as noted above, more recent empirical studies have failed to find an effect even of that size. Nevertheless, given the empirical evidence that prevailing wages tend to be higher than nonprevailing wages and that labor costs are a significant portion of overall project costs, DLS believes that it is reasonable to expect that the prevailing wage requirement adds between 2% and 5% to the cost of a public works project. Given the inconsistency and inconclusiveness of the empirical research, however, actual effects may vary by project, with some projects exhibiting higher cost differences and others experiencing negligible differences.