HB 37

Department of Legislative Services

Maryland General Assembly
2021 Session

FISCAL AND POLICY NOTE
Enrolled - Revised

House Bill 37 (Delegate Valderrama)
Economic Matters Finance

Procurement - Prevailing Wage - Applicability

This bill expands the applicability of the State's prevailing wage law to include (1) a public work project contract with a value of $250,000 or more (instead of $500,000 or more) and (2) a public work project for which State funds constitute at least 25% of the construction costs (instead of at least 50% of construction costs). Legislative bond initiatives that receive State funds in the capital budget are exempt from the bill's requirements. The bill only applies to a public work project contract executed on or after October 1, 2021.

Fiscal Summary

State Effect: General fund expenditures increase by $51,400 in FY 2022 to enforce the bill's provisions; out-year expenditures reflect annualization and ongoing operating costs. Special fund revenues increase meaningfully from anticipated contributions to the State Apprenticeship Training Fund (SATF), although a precise estimate is not feasible. No effect on total State capital expenditures, but the cost of some public work projects may increase; therefore, fewer projects may be funded in a given year.

(in dollars)	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
SF Revenues	-	-	-	-	-
GF Expenditure	$51,400	$59,200	$60,800	$62,900	$65,100
Net Effect	($51,400)	($59,200)	($60,800)	($62,900)	($65,100)

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

Local Effect: No effect on local capital funding available for public work projects, but the cost of some projects may increase, resulting in fewer projects receiving funding in a given year. No effect on local revenues.

Small Business Effect: Minimal.

Analysis

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

Chapter 687 of 2009 established SATF as a special, nonlapsing fund, and requires contractors and some subcontractors on public work contracts that are subject to the prevailing wage law to either (1) participate in an apprenticeship training program; (2) make payments to a registered apprenticeship program or to an organization that operates registered programs for the purpose of supporting the programs; or (3) make specified payments to the fund. The fund's revenues consist entirely of payments made by contractors and penalties collected due to violations of the statutory provisions.

State Revenues: By virtue of being required to pay prevailing wages under the bill, additional public work projects also have to comply with the requirements of Chapter 687. As many of the affected projects are likely to be small and/or managed by nonprofit organizations with little experience with capital construction, it is assumed that many projects elect to contribute to SATF in lieu of participating in or contributing to a registered apprenticeship program. Therefore, annual special fund revenues for SATF likely increase meaningfully beginning in fiscal 2022, although a precise estimate cannot be made due to the uncertainty regarding the number and size of projects that will elect to contribute each year.

State Expenditures: The bill affects certain types of public work projects not currently required to pay prevailing wages, including:

- contracts on State projects with a value of at least $250,000 but less than $500,000;
- local government nonschool projects that are funded with between 25% and 50% State funds (inclusive) and have contracts valued at $250,000 or more;
- miscellaneous grant programs in the capital budget that meet the bill's thresholds; and
- school construction projects with 25% or more State funding and contracts valued at between $250,000 and $500,000.

Lowering the contract threshold to $250,000, in combination with requiring all such projects (except legislative bond initiatives) that receive at least 25% State funds to pay prevailing wages means that a substantial number of miscellaneous grant recipients and State and local projects that currently do not pay prevailing wages, because they do not meet current thresholds, must pay them under the bill's new thresholds. Based on earlier estimates provided by the Division of Labor and Industry (DLI) within the Maryland Department of Labor, which enforces the prevailing wage requirement, the Department of

Legislative Services (DLS) estimates that about 200 additional projects must pay prevailing wages each year. The fiscal 2022 capital budget, as enacted, alone has about 150 miscellaneous grant projects; it is anticipated that a substantial number of those qualify for the payment of prevailing wages.

DLI and the Department of General Services (DGS) both have increased oversight or enforcement roles as a result of the bill; however, only DLI requires additional staff to carry out its duties. As noted in the appendix, DLI currently oversees more than 1,000 prevailing wage projects with five investigators, for an average of about 200 projects per investigator. Given the anticipated increase of 200 projects mentioned above, DLI requires one additional investigator to handle the enforcement responsibilities.

Therefore, general fund expenditures increase by $51,416 in fiscal 2022, which accounts for the bill's October 1, 2021 effective date. This estimate reflects the cost of hiring one wage and hour investigator to enforce the prevailing wage requirement for public work projects that are required to pay prevailing wages under the bill. It includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Position	1.0
Salary and Fringe Benefits	$43,410
Operating Expenses	8,006
Total FY 2022 State Expenditures	**$51,416**

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

The DGS Capital Grants Program oversees grantees who receive miscellaneous capital grants from the State to support the construction of a building or other structure. Typically, these projects do not receive enough from the State to reach the 50% funding threshold in current law, but under the bill, many will be required to pay prevailing wages if they award construction contracts that reach the bill's thresholds. DGS advises that it will require eligible grantees to certify that they are complying with prevailing wage requirements but otherwise will not provide additional enforcement or oversight. Therefore, DGS does not require additional staff. DLS notes that past experience has shown that many grantees have little experience managing large capital construction projects and even less familiarity with State requirements. Therefore, many will require extensive technical assistance and guidance from DGS and DLI; however, that assistance can likely be provided with existing resources and the additional investigator provided to DLI.

Project Costs

As noted in the appendix, the total costs of projects required to pay prevailing wages under the bill likely increase by between 2% and 5% overall, although individual projects may experience greater or lesser increases. These increases do not affect overall State capital funding, which is established annually by the Governor and General Assembly through the capital budget process. However, it may result in fewer projects being funded each year.

Additional Information

Prior Introductions: None.

Designated Cross File: SB 35 (Senator Feldman) - Finance.

Information Source(s): City of Bowie; Caroline, Montgomery, and Prince George's counties; Maryland Department of Labor; Department of General Services; Maryland Association of Counties; Maryland Municipal League; Department of Legislative Services

Fiscal Note History: First Reader - January 26, 2021
rh/ljm Third Reader - March 22, 2021
Revised - Amendment(s) - March 22, 2021
Enrolled - April 9, 2021
Revised - Amendment(s) - April 9, 2021
Revised - Budget Information - April 9, 2021

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;
- any other public work for which at least 50% of the money used for construction is State money; and
- specified projects in tax increment financing districts if the local governing body approves of the application of prevailing wages.

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 Maryland Department of Labor (MDL).

The University System of Maryland (USM), Morgan State University (MSU), St. Mary's College of Maryland, and the Maryland Stadium Authority (MSA) are all exempt from the prevailing wage law. However USM, MSU, and MSA all voluntarily comply with prevailing wage requirements for contracts that exceed the $500,000 threshold.

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, thereby requiring the vast majority of public school construction projects in the State 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. MDL advises that, during fiscal 2020, its prevailing wage unit monitored 1,091 projects, down slightly from 1,120 projects in fiscal 2019, but significantly up from 496 in fiscal 2014. To accommodate the increase in projects, the number of prevailing wage investigators increased in fiscal 2016 from three to six; there are currently five investigators.

Six Maryland jurisdictions – Allegany, Baltimore, 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) has reviewed 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 MDL (at the time, the Department of Labor, Licensing, and Regulation) 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 through 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. An independent analysis of the Maryland side-by-side bid data concluded that factors other than prevailing wages, including bid timing and the level of competition for the bids, accounted for most of the differences between the prevailing wage and nonprevailing wage bids.

A series of large-scale studies completed about 10 years ago 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 U.S. 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.