SB 259

Department of Legislative Services

Maryland General Assembly
2022 Session

FISCAL AND POLICY NOTE
Third Reader

Senate Bill 259 (Senator Feldman, *et al.*)

Finance Economic Matters

Procurement - Prevailing Wage - Applicability

This bill applies the State's prevailing wage requirements to "mechanical systems service contracts," as defined by the bill, that are part of public work contracts with a value that exceeds a specified threshold in federal law, which is currently $2,500. A "mechanical systems service contract" is defined as a contract for (1) heating, ventilation, and air conditioning (HVAC), including ductwork; (2) refrigeration systems; (3) plumbing systems, as specified; (4) electrical systems, as specified; and (5) elevator systems, as specified. "Construction" is expanded to explicitly include such services.

Fiscal Summary

State Effect: General fund expenditures increase by *at least* $571,400 in FY 2023 for implementation and enforcement; out-years reflect annualization, annual increases, and elimination of one-time costs. State expenditures (all funds) may also increase significantly beginning in FY 2023 for ongoing maintenance of State buildings and other public works, but a reliable estimate is not feasible. The application of existing penalties is not expected to have a material effect on general fund revenues.

(in dollars)	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027
Revenues	$0	$0	$0	$0	$0
GF Expenditure	571,400	494,100	507,700	520,700	534,600
Net Effect	($571,400)	($494,100)	($507,700)	($520,700)	($534,600)

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

Local Effect: Local expenditures may increase significantly for ongoing maintenance of public works owned by local governments, but a reliable estimate is not feasible. No effect on revenues. **This bill may impose a mandate on a unit of local government.**

Small Business Effect: Meaningful.

Analysis

Current Law: For an overview of the State's prevailing wage requirements, please see the **Appendix – Maryland's Prevailing Wage Law**.

A "public work contract" is defined as a contract for construction of a public work.

State Expenditures:

Mechanical Systems Service Contracts Costs

As prevailing wage rates for mechanical service technicians do not exist, it is difficult to determine whether and to what extent the bill has an effect on State expenditures for these services. Unlike construction workers, such service technicians are generally required to be licensed and insured, so market wage rates for licensed mechanical technicians are generally high. Thus, it is not clear whether the payment of prevailing wages meaningfully increases payments to them. To the extent that they do, project costs likely increase, potentially significantly, but a reliable estimate is not feasible in the absence of more data. As ongoing maintenance costs are operating, rather than capital, expenditures, State expenditures (all funds) may increase substantially.

Administration and Enforcement

The bill dramatically expands the application of prevailing wage requirements in two ways. First, it requires payment of prevailing wages for ongoing service contracts, not just construction contracts. Second, it requires payment of prevailing wages for mechanical service contracts valued at more than $2,500, instead of the $250,000 threshold under current law. The Maryland Department of Labor (MDL) advises that this expansion presents implementation challenges in addition to increasing expenditures for administration and enforcement, and the Department of Legislative Services concurs.

Payment of prevailing wages is already required for the installation of mechanical building systems during the construction of a public work project, so the bill has no effect on construction costs. However, service contracts are not covered by current law. The bill, therefore, extends requirements to pay prevailing wages for ongoing maintenance of the mechanical systems for the life of a building or other public work. MDL advises that its current system used to determine prevailing wage rates collects data only for construction workers (installers) but does not collect wage information for service technicians. Therefore, MDL needs to update its online system to collect data on wages paid for service contracts and then analyze that data to establish appropriate prevailing wages for each jurisdiction in the State.

Furthermore, the bill expands MDL's enforcement responsibility. Each building constructed likely has multiple mechanical systems (HVAC, plumbing, electrical, etc.), each with its own service contract. Therefore, the number of contracts monitored by MDL to ensure proper payment of prevailing wages increases significantly. This increase is mitigated somewhat by the fact that most service visits are limited in duration and scope, requiring less work than a major construction contract that can last several years. Nevertheless, the increase in workload is significant given the large number of affected contracts. MDL likely needs to develop new enforcement guidelines for service contracts given the different scope and duration of these contracts compared with construction contracts.

Therefore, general fund expenditures increase by *at least* $571,404 in fiscal 2023, which accounts for the bill's October 1, 2022 effective date. This estimate reflects the cost of hiring five new wage and hour investigators, an administrative aide, and an administrator to oversee enforcement of service contracts. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses, including one-time costs to upgrade the online wage database and other enforcement-related systems.

Positions	7
Salaries and Fringe Benefits	$353,315
Information Technology Upgrades	150,000
Operating Expenses	68,089
Total FY 2023 State Expenditures	**$571,404**

Future year expenditures reflect full salaries with annual increases and employee turnover as well as annual increases in ongoing operating expenses. This staffing complement reflects a doubling of staff, which may not be sufficient to handle the significantly expanded enforcement duties under the bill. Even more additional staff may be necessary.

Local Expenditures: Local operating expenditures for ongoing maintenance of public work projects may similarly increase, as discussed above for State projects.

Small Business Effect: Many mechanical service companies are small businesses, and they will have to pay their technicians prevailing wage rates for work on public works. In most cases, they will pass on any increase in wages to the public body that owns the public work, so there is no financial effect on the businesses. However, the bill presents administrative challenges to small businesses that provide mechanical services. First, to the extent that prevailing wages are more than their usual wage rates, they will have to maintain two separate wage scales for work on private and public sites. Second, they will have to comply with wage reporting requirements that are the foundation of prevailing wage enforcement efforts. Some small businesses find these requirements to be administratively burdensome.

Additional Comments: Any effect on apprenticeships, including payments to the State Apprenticeship Training Fund, due to expansion of the requirement for payment of prevailing wages has not been factored into this analysis.

Additional Information

Prior Introductions: None.

Designated Cross File: HB 611 (Delegate Valderrama, *et al.*) - Economic Matters.

Information Source(s): Maryland Association of Counties; Maryland Municipal League; Public School Construction Program; Department of General Services; Maryland Department of Labor; Department of Public Safety and Correctional Services; Board of Public Works; Maryland Department of Transportation; Department of Legislative Services

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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;
- any public work for which at least 25% 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 $250,000 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; (2) specified construction projects carried out by public service companies under order of the Public Service Commission; or (3) local House or Senate initiatives that receive State funds in the capital budget.

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 $250,000 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. Chapters 57 and 58 of 2021 lowered the State funding threshold for all public works projects (including school construction) to 25% of total construction costs and lowered the contract value threshold for payment of prevailing wages to $250,000; however, legislative bond initiatives that receive State funds in the capital budget are exempt from the requirement to pay prevailing wages.

The number of prevailing wage projects has risen dramatically in recent years. MDL advises that, during fiscal 2021, its prevailing wage unit monitored 941 projects, down slightly from 1,091 projects in fiscal 2020, but significantly higher than 496 in fiscal 2014. To accommodate the increase in projects, the number of prevailing wage investigators increased in fiscal 2016 from three to six; as of January 2022, there are four investigators, with a fifth investigator in the latter stages of recruitment.

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, but beginning in fiscal 2023, the county will pay prevailing wages on all school construction projects, regardless of the level of State or county participation.

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."

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.

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 (with materials and site costs making up most of the rest). Therefore, a 10% gap between prevailing wages and market wages could theoretically increase total contract costs by about 2.5%, and a 20% gap in wages could increase total contract costs by about 6%. 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.