Department of Legislative Services

Maryland General Assembly
2000 Session

FISCAL NOTE

House Bill 819 (Delegate Kittleman, *et al.*)
Economic Matters

Prevailing Wage Law - Repeal

This bill repeals the State's prevailing wage law for public works contracts, and removes the reference to the Advisory Council on Prevailing Wage Rates from the Maryland Program Evaluation Act.

Fiscal Summary

State Effect: General fund revenues would decrease by about $50,000 annually. General and special fund expenditures would decrease by an estimated $8.5 to $42.3 million in FY 2001, which reflects the bill's October 1, 2000, effective date, and $11.3 to $56.4 million on an annualized basis. Future year expenditure decreases cannot be reliably estimated at this time but could be substantial.

Local Effect: In aggregate, local expenditures could decrease by $4.2 to $21.2 million in FY 2001, which reflects the bill's effective date. Local revenues would not be affected.

Small Business Effect: Meaningful.

Analysis

Current Law: Title 17, Subtitle 2, of the State Finance and Procurement Article outlines the definitions, procedures, and requirements of Maryland's prevailing wage law. The prevailing wage law applies to any public works contract when State funds are used to finance at least 50% of the construction costs of a particular project. Public school projects are subject to prevailing wages if the State funding contribution is at least 75% of total project funding. The prevailing wage law does not apply to projects with a cost of less than $500,000.

By definition, prevailing wages are the hourly wage rates paid in the locality in which the construction work is to be performed. If 50% or more of all workers in a trade are paid exactly the same rate, then that rate is considered to be the prevailing wage. If not, then 40% or more of the employees for each work classification must be paid the same rate in order for the rate to qualify as prevailing. If less than 40% receive the same rate, then a weighted average is calculated and used as the prevailing wage. Prevailing wages are based on hourly salary levels, as well as employer benefit contributions.

The State share of eligible costs for school construction is 75% or less in all jurisdictions except Somerset, where it is 80%. In no jurisdiction is the State share less than 50%.

Under the Maryland Program Evaluation Act, the Department of Legislative Services is required to evaluate the agencies specified in statute every ten years. The agencies subject to review are automatically terminated unless legislative action is taken to re-authorize them. A preliminary review of the Advisory Council on Prevailing Wages would be done in 2001, and without re-authorization, the agency will automatically terminate on July 1, 2004.

State Revenues: Under current law the Commissioner of Labor and Industry can assess liquidation damages against any employer who fails to pay the prevailing wage or fails to provide timely disclosure of payroll records. If the prevailing wage law is repealed, it is estimated that general fund revenue would decline by about $50,000 annually, which reflects the average annual amount of a five-year forecast for liquidation damages collected by the commissioner.

State Expenditures: State expenditures could decrease in fiscal 2001 due to: (1) the elimination of the Prevailing Wage Unit of the Division of Labor and Industry; and (2) the reduction in construction costs for contracts which are no longer subject to the State prevailing wage law.

Elimination of the Prevailing Wage Unit

Repealing the prevailing wage law would eliminate the need for the Prevailing Wage Unit and reduce general fund expenditures accordingly. Based on the unit's fiscal 2001 budget allowance, expenditures would decrease by $236,969. This amount reflects salaries, fringe benefits, ongoing operating expenses, and an October 1, 2000, effective date.

Reduction in Construction Costs

There are only two studies specific to the impact of prevailing wages in Maryland, and both are on school construction.

A study on the impact of prevailing wages was recently prepared for the Prince George's County Council by Dr. Mark Prus. The author concluded that building a school in a prevailing wage jurisdiction in Maryland would cost 1.9% more than building the same school in a non-prevailing wage jurisdiction, and that this result was not statistically significant.

A Department of Legislative Services (DLS) study in 1989 concluded that the prevailing wage increases project costs by 5% to 15%, and that the actual impact depends upon the type of project, labor costs as a share of total costs, and market conditions. In 1995, DLS reviewed the 1989 study and current data, and concluded that the 5% to 15% range was still valid. Although the DLS study was done before the current economic boom for the construction industry, it was done at the peak of the construction boom of the 1980s.

According to the U. S. Bureau of Economic Analysis, since the DLS study was conducted the Maryland Gross State Product from the construction industry has grown by 6.7% in nominal terms and labor compensation paid by the industry has grown by 15%. Because the growth in compensation has outpaced that of the industry and the current boom does not appear to have peaked yet, the differential between the prevailing wage and the current wage should be lower than found in the DLS study.

The two studies indicate that prevailing wages could add 2% to 15% to the cost of a project. Because of the change in compensation since the DLS study, the 15% may be reduced to as low as 10% in today's market.

The State's proposed capital program for fiscal 2000 is approximately $2.54 billion, including transportation projects. Approximately two-thirds of the capital program is paid by the State and one-third of the capital program is paid by local jurisdictions. However, only one-third of the capital program would be affected by repealing the State's prevailing wage law because the following items are exempt or otherwise excluded: (1) any portion of a project funded with federal money; (2) grants to private entities; (3) land, design, and equipment; and (4) projects below $500,000.

Therefore, repealing the State's prevailing wage law as of October 1, 2000, would affect approximately $847 million in the State's 2001 capital program. Assuming that prevailing wages increase costs by 2% to 10%, construction expenditures would be reduced by $8.5 to $42.3 million ($11.3 to $56.4 million on an annualized basis). Out-year expenditure reductions would depend upon the State's capital program in any given year and cannot be reliably projected.

Any savings realized in construction costs could be used to fund additional capital projects or to reduce the State's debt authorization. If debt authorization is reduced, the State would realize an additional savings related to the cost of servicing the debt. The savings would depend on a number of factors, including the reduction in construction costs and the interest rate. For example, assuming: (1) two-thirds of general obligation debt is for construction; (2) the savings in construction costs were 5%; (3) authorized bonds are issued over a five-year period; (4) bonds have a 15 year maturity and no principal is paid in the first two years; and (5) the interest rate is 5.25%, the potential savings in interest and principal would be $59.5 million for a ten-year period.

Local Expenditures: Local expenditures would decrease to the extent that repealing the State's prevailing wage law would reduce construction costs and debt service. Based on the State's 2001 capital program and the 2% to 10% increase in costs due to prevailing wages, local expenditures would decrease by $4.2 to $21.2 million ($5.6 to $28.2 million on an annualized basis) in fiscal 2000, which reflects the October 1, 2000, effective date.

Small Business Effect: The majority of the contractors and subcontractors in the State are small businesses. It is assumed that the majority of the businesses hired for State projects that require prevailing wages are also small businesses. This bill could have a meaningful effect on these businesses to the extent that their expenditures for wages paid in the performance of State contracts are reduced.

Additional Comments: In fiscal 1999 the Prevailing Wage Unit recovered $224,631 in restitution for employees who were paid less than the prevailing wage.

It should be noted that various studies have been conducted in other states that conclude that the prevailing wage law actually reduces government expenditures on construction projects. However, prevailing wage laws differ significantly among states. Furthermore, there are various studies that show that the prevailing wage law increases State expenditures.

Additional Information

Prior Introductions: This bill was introduced as HB 404 in the 1999 session, HB 51 in the 1998 session, HB 720 in the 1997 session, and HB 286 in the 1996 session. Each bill received an unfavorable report from the House Economic Matters Committee.

Cross File: None.

Information Source(s): Department of Labor, Licensing, and Regulation (Division of Labor and Industry); Department of Budget and Management; Department of Health and Mental Hygiene; Department of Public Safety and Correctional Services (Division of Correction); State Highway Administration; *Prevailing Wage Laws and School Construction Costs*, Dr. Mark J. Prus, PhD., SUNY Cortland; *Maryland's Prevailing Wage Law: A Study of Costs and Benefits*, Department of Legislative Services

Fiscal Note History: First Reader - March 6, 2000
nlr/jr

Analysis by: Christine A. Scott

Direct Inquiries to:
John Rixey, Coordinating Analyst
(410) 946-5510
(301) 970-5510