

Department of Legislative Services  
Maryland General Assembly  
2006 Session

FISCAL AND POLICY NOTE

Senate Bill 27  
Finance

(Senator Kittleman)

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Procurement - Prevailing Wage - School Construction

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This bill raises the share of a school construction project that must be funded by the State before the prevailing wage law applies from 50% to 75%.

The bill takes effect July 1, 2006.

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Fiscal Summary

**State Effect:** Minimal. The State would realize marginal savings from school construction projects only if actual project costs were below projected costs, which rarely occurs. It is assumed that any savings would be reallocated to other projects and would not result in a net decrease in school construction expenditures.

**Local Effect:** Local expenditures could decrease significantly because fewer school construction projects would have to pay higher prevailing wages. Total savings could be less for two reasons. First, this estimate assumes that prevailing wages are 5% higher than market wages, as estimated in 2004, but prevailing wages may actually be comparable to market wages as construction costs have risen sharply since then. Second, more projects than assumed may fall below the current 50% State share threshold in those jurisdictions with a State share above 50%.

**Small Business Effect:** Minimal. School construction contractors that are required to pay prevailing wages pass along those higher costs to the State and local school systems.

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## Analysis

**Current Law:** School construction projects are subject to the prevailing wage law if 50% or more of total construction costs are paid by the State. However, the prevailing wage law does not apply to projects that cost less than \$500,000.

Prevailing wages are defined in Maryland statute as the wages paid to 50% of workers in a given locality who perform the same or similar work on projects that resemble the proposed public work 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 Commissioner of Labor and Industry is responsible for determining prevailing wages for each public work project and job category.

**Background:** The purpose of the prevailing wage provision is to prevent bidders on public works contracts from bringing in lower-wage labor from other areas to work on local construction projects, thereby underbidding local contractors.

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 exceeding \$500,000. 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.

Several Maryland jurisdictions (Allegany County, Baltimore City) have local prevailing wage laws requiring all public work projects in the jurisdiction to pay prevailing wages, including school construction.

The Task Force to Study Public School Facilities, which was established by Chapter 288 of 2002 and submitted a final report in February 2004, recommended a new methodology for determining State and local shares of school construction funding. The method uses numerous local factors including local wealth, local needs, and past local effort. In general, the State share is the highest in jurisdictions that have the least financial capacity to pay for school construction projects.

**Exhibit 1** shows the State share of eligible school construction costs for all Maryland jurisdictions for fiscal 2007 and 2008.

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**Exhibit 1**  
**State Share of Eligible School Construction Costs,**  
**Fiscal 2006 to 2008**

50%	Anne Arundel, Baltimore, Kent, Montgomery, Talbot, Worcester
58%	Howard
65%	Carroll, Harford, Washington
69%	Calvert
70%	Cecil, Charles, Garrett, Queen Anne's
72%	Frederick, St. Mary's
75%	Prince George's*
77%	Dorchester
81%	Wicomico
89%	Caroline
90%	Allegany
97%	Baltimore City, Somerset

\*For fiscal 2006-08, the State match for Prince George's County is 75% for funding allocated up to \$35 million, and 69% for funding allocated in excess of \$35 million.

Source: Public School Construction Program

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**Local Fiscal Effect:** In fiscal 2007 and 2008, the State share of eligible school construction costs ranges from 50% to 75% in all but six jurisdictions. The six jurisdictions that require State shares higher than 75% are: Allegany, Caroline, Dorchester, Somerset, and Wicomico counties, and Baltimore City.

A school construction project is subject to the prevailing wage provision if the State's share of total construction costs, including both eligible and ineligible costs, exceeds 50%. Costs that are ineligible for State funding include items like movable objects (*e.g.*, bookcases) and planning and design fees. Since total construction costs are typically higher than eligible construction costs, the State often pays less than 50% of total school construction costs in jurisdictions that require a 50% State match of eligible costs. Therefore, almost all school construction projects in jurisdictions with a 50% State match are not required to pay the prevailing wage. It is assumed that the bill has no effect in the six jurisdictions that have a 50% State share (Anne Arundel, Baltimore, Kent, Montgomery, Talbot, and Worcester). Moreover, if a contract award is substantially higher than the maximum State cost estimated by the Interagency Committee on School

Construction (IAC), some school construction projects in jurisdictions with higher State matches may not have to pay the prevailing wage under current law. This is because only local funds may be used to cover the project's higher-than-projected costs, and that may drop the State share of total costs below 50%.

Determining the fiscal impact of the prevailing wage requirement has been complicated by recent dramatic increases in construction costs, including labor rates. Research conducted in 2004 by Dr. Yale Stenzler, former executive director of the State's Public School Construction Program (PSCP), concluded that from fiscal 2001 to 2003, prevailing wage rates increased school construction costs by 5% to 10%. Since then, the prices of fuel, building supplies, and construction labor have risen steeply, adding between 12% and 20% to the cost of school construction. Although the rate of increased construction costs has slowed, the demand for building supplies and labor could remain high as the Gulf region continues rebuilding after Hurricane Katrina. These increased costs have clouded the gap between market wage rates and prevailing wage rates. PSCP advises that in an environment of escalating construction costs, market wage rates can equal or exceed prevailing wages.

Perhaps the most promising strategy for estimating the impact of prevailing wage rates on school construction costs is to compare project bids that provide both prevailing wage and market wage rates. For several years, local school districts have been allowed to solicit bids for the same project with both estimates. They have occasionally solicited these side-by-side bids to help them determine whether they want to accept the full State match (and be subject to the prevailing wage), or a lesser State match without being subject to the prevailing wage. However, PSCP reports that local school systems have not asked for many side-by-side bids since construction costs began their steep rise.

Nevertheless, in the absence of more recent data, it seems prudent to assume that prevailing wages continue to exceed market wages, and reasonable to use the lower end of Dr. Stenzler's estimated impact, or 5%. Therefore, raising the prevailing wage threshold could reduce total school construction costs by 5%. All of these savings would be realized by the local jurisdictions because the increased cost due to prevailing wages is borne entirely by local jurisdictions. Jurisdictions with school construction State shares above 75% would remain subject to the prevailing wage provision and receive no savings.

*For illustrative purposes*, the Department of Legislative Services (DLS) has reviewed the initial list of school construction projects recommended by the IAC for fiscal 2007 to identify the school construction projects most likely to fall between the 50% prevailing wage threshold in current law and the proposed 75% threshold. **Exhibit 2** contains a profile of the 31 projects identified by DLS. The list does not include ongoing projects

that began in prior years, and should be viewed as a working guide because the actual State share for these projects will not be known until they are under contract.

As Exhibit 2 shows, raising the prevailing wage threshold could reduce local school construction costs by \$7.9 million for these 31 projects.

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**Exhibit 2**  
**Fiscal 2007 Public School Construction Projects**  
**Not Expected to Have to Pay Prevailing Wage Under SB 27**  
**(\$ in thousands)**

<b>County</b>	<b>Projects Requiring Prevailing Wage Under Current Law</b>	<b>Total Project Cost</b>	<b>Local Funding</b>	<b>State Funding</b>	<b>Potential Savings from SB 27*</b>
Calvert	8	\$39,505	\$12,308	\$27,197	\$1,976
Carroll	5	25,290	11,260	14,030	1,264
Charles	2	2,264	911	1,353	113
Frederick	1	32,358	9,060	23,298	1,618
Garrett	1	1,331	421	910	67
Harford	1	1,510	567	943	76
Howard	1	1,091	467	624	55
Prince George's	9	25,114	7,188	17,926	1,257
St. Mary's	2	28,301	8,316	19,985	1,415
Washington	1	672	224	448	34
<b>Total</b>	<b>31</b>	<b>\$157,436</b>	<b>\$50,722</b>	<b>\$106,714</b>	<b>\$7,875</b>

\*Assumes a 5% savings on the total project cost without prevailing wage.

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**Additional Information**

**Prior Introductions:** SB 80 of 2003 received an unfavorable report from Finance. HB 396 of 2004 received an unfavorable report from Economic Matters.

**Cross File:** None.

**Information Source(s):** Maryland Department of Planning, Department of General Services, Maryland State Department of Education, Public School Construction Program, Department of Legislative Services

**Fiscal Note History:** First Reader – February 15, 2006  
nas/rhh

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