HB 707

Department of Legislative Services

Maryland General Assembly
2011 Session

FISCAL AND POLICY NOTE

House Bill 707 (Delegate Krebs, *et al.*)
Economic Matters

State Finance and Procurement - Prevailing Wage Rates - Amount of Public Work Contracts

This bill raises, from $500,000 to $2.0 million, the threshold for public works contracts above which contractors and subcontractors must pay their employees a prevailing wage.

Fiscal Summary

State Effect: General fund expenditures by the Department of Labor, Licensing, and Regulation (DLLR) decrease by $135,000 in FY 2012 due to diminished enforcement activities. Out-year savings reflect annualization and inflation. Costs for individual State public works projects that are worth between $500,000 and $2.0 million may decrease by between 2% and 3% because they no longer have to pay prevailing wage rates. There is no assumed change in State capital expenditures, which are established annually by the Governor and General Assembly; instead it is assumed that more projects receive funding due to the reduced costs of some public works projects.

(in dollars)	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
Revenues	$0	$0	$0	$0	$0
GF Expenditure	(135,000)	(182,200)	(189,800)	(197,700)	(205,900)
Net Effect	$135,000	$182,200	$189,800	$197,700	$205,900

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

Local Effect: Costs for individual public works projects that are worth between $500,000 and $2.0 million and that are otherwise currently subject to the prevailing wage law may decrease by between 2% and 3% because they no longer have to pay prevailing wage rates. This does not include four counties that have their own local prevailing wage laws. No change in overall local government capital expenditures is assumed; instead more local capital projects receive funding.

Small Business Effect: Minimal.

Analysis

Current Law: Contractors working on eligible public works projects must pay their employees the prevailing wage rate. Eligible public works projects are those valued at more than $500,000 and carried out by:

- the State; or
- a political subdivision, agency, person, or entity for which at least 50% of the project cost is paid for by State funds.

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. The State prevailing wage rate does not apply to any part of a public works project funded with federal funds for which the contractor must pay the prevailing wage rate determined by the federal government.

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 DLLR Commissioner of Labor and Industry is responsible for determining prevailing wages for each public works project and job category, subject to the advice and recommendations of a six-member advisory council appointed by the Governor.

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 employee who is paid less than 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 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.

Background: 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 exceeding $500,000 (effective July 1, 1970). Adjusted for inflation, the threshold would currently be $2.8 million. 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.

DLLR advises that its prevailing wage unit currently monitors about 160 prevailing wage projects throughout the State, including those procured by local governments. This number is higher than totals reported in recent years, which have tended to be between 110 and 130 projects. In 2010, the unit investigated 375 project sites for prevailing wage compliance and recovered $360,000 in unpaid wages on behalf of laborers.

Four Maryland jurisdictions – Allegany, Montgomery (beginning in July 2009), and Prince George's counties and Baltimore City – have local prevailing wage laws requiring public works projects in the jurisdiction to pay prevailing wages, including school construction.

State Fiscal Effect: Raising the threshold for prevailing wage requirements reduces expenditures by DLLR to enforce the law. Assessing the short- and long-term effects on the State's construction contract costs has been complicated by the recent downturn in the construction industry.

Administrative Costs: The prevailing wage unit within DLLR's Division of Labor and Industry enforces employers' compliance with the prevailing wage. The proposed fiscal 2012 State budget for the unit includes 11 full-time equivalent (FTE) regular positions (of which one is vacant) and a total budget of almost $705,000. This includes five investigators who directly monitor contractor compliance with the prevailing wage law. DLLR advises that of the projects it currently monitors, approximately 40% are worth more than $2.0 million. The Department of Legislative Services (DLS) assumes that two investigators and one administrator who runs the unit must be retained to continue monitoring the remaining prevailing wage projects and the full-time assistant Attorney General assigned to the unit is reduced to a half-time position.

Therefore, general fund expenditures by DLLR decrease in fiscal 2012 by $134,964 to eliminate three investigator positions and a 0.5 FTE assistant Attorney General, which accounts for the bill's October 1, 2011 effective date. Savings continue to accrue in the out years, subject to annualization and inflation.

Contract Costs: Public works contracts worth between $500,000 and $2.0 million are no longer required to pay workers a prevailing wage under the bill. This has the potential to decrease labor costs, and potentially total contract costs, for those projects, but recent research suggests that the effects on contract costs are uncertain.

For recent prior versions of other prevailing wage bills, DLS conducted an extensive review of research on the effect of prevailing wage laws on the cost of public works contracts and found inconsistent results. 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 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%. However, an increasing number of studies carried out in the past 10 years have found no statistically significant effect on contract costs.

Labor costs, including benefits and payroll taxes, represent between 20% and 30% of total construction costs. Therefore, a 10% gap between prevailing wages and market wages would increase total contract costs by between 2% and 3%. As noted above, however, most recent studies have failed to find an effect even of that size. Among the reasons cited in the research for the absence of a cost effect include:

- the gap between prevailing wages and market wages has been closing due to the construction boom in the early and middle part of the past decade;
- 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.

Other studies have examined the revenue effects of prevailing wage laws. A recent study in Missouri determined that prevailing wages yielded substantial sales and income tax revenue for the State.

The recent virtual collapse of the construction sector makes speculation about the effects of the prevailing wage on contract costs difficult. Although research over the past decade indicates that there may be no measurable effect on contract costs, the conditions that existed when that research was conducted no longer exist. There is no reliable information about the relationship between prevailing and market wages in the current economic environment. An expanding pool of available labor could widen the gap between market and prevailing wages, or it could exert downward pressure on all wages, yielding no gap between the two wage rates. Therefore, the Department of Legislative Services estimates that exempting more projects from the prevailing wage requirement may reduce their total cost by between 2% and 3%, subject to updated research on construction wage rates in the current depressed economic environment.

However, reduced costs for some public works projects does not reduce the State's overall capital budget, which is established annually by the Governor and General Assembly. To the extent that savings on some public works projects are realized, State funding may be available for more projects.

In some cases, especially for transportation projects that receive federal funds, the federal prevailing wage requirement may replace the State requirement, yielding little or no savings for those projects.

Local Revenues: Local public works projects that are worth between $500,000 and $2.0 million and that receive at least half of their funds from the State no longer have to pay prevailing wage rates. This does not include Allegany, Montgomery, and Prince George's counties and Baltimore City, which have their own local prevailing wage laws. Based on the research cited above, and subject to the same caveats, total project costs for those projects may decrease by between 2% and 3%.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Garrett, Harford, and Montgomery counties; Department of Budget and Management; Maryland Department of Planning; Department of General Services; Department of Labor, Licensing, and Regulation; Public School Construction Program; Maryland Department of Transportation; Department of Legislative Services

Fiscal Note History: First Reader - March 21, 2011
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