HB 650

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FISCAL AND POLICY NOTE
Revised

House Bill 650 (Montgomery County Delegation and Prince George's County Delegation)

Economic Matters and Environmental Matters Finance

Washington Suburban Sanitary Commission - Prevailing Wage
MC/PG 112-13

This bill requires the payment of prevailing wages on *any* public works contract entered into by the Washington Suburban Sanitary Commission (WSSC) that has a contract value of at least $500,000, regardless of funding source.

Fiscal Summary

State Effect: General fund expenditures by the Department of Labor, Licensing, and Regulation (DLLR) increase by $92,900 in FY 2014 to enforce WSSC compliance with the prevailing wage law. Out-year costs reflect annualization, inflation, and employee turnover. No effect on revenues.

(in dollars)	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Revenues	$0	$0	$0	$0	$0
GF Expenditure	92,900	116,200	121,400	126,900	132,600
Net Effect	($92,900)	($116,200)	($121,400)	($126,900)	($132,600)

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

Local Effect: The bill may increase the cost of future WSSC public works projects by between 2% and 5%. Potential minimal increase in WSSC revenues due to the payment of liquidated damages. **This bill imposes a mandate on a unit of local government.**

Small Business Effect: Minimal. Construction contractors that are required to pay prevailing wages generally pass along the higher costs to the governmental agency.

Analysis

Current Law: 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. Contractors working on eligible public works projects must pay their employees the prevailing wage rate. Eligible public works projects are those 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.

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 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 State 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 (either the State or the local government that procured the project) in the amount of $20 a day for each laborer 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: WSSC is among the largest water and wastewater utilities in the country, providing water and sewer services to 1.8 million residents in Montgomery and Prince George's counties. It has more than 460,000 customer accounts, serves an area of around 1,000 square miles, and currently employs more than 1,500 people. The agency operates three reservoirs, two water filtration plants, and six wastewater treatment plants. The six wastewater treatment facilities, as well as the Blue Plains Advanced Wastewater Treatment Plant, handle as much as 180 million gallons per day. The commission maintains nearly 5,600 miles of water main lines and more than 5,400 miles of sewer main lines. According to WSSC's fiscal 2013 budget, approved expenditures for capital projects in fiscal 2013 total $788.9 million, of which $397.0 million is for contract work. This is a substantial increase from actual expenditures in fiscal 2011, which totaled $240.3 million, of which $98.2 million was for contract work. In fiscal 2013, wastewater treatment projects are projected to make up 67.0% of total capital spending, followed by 30.5% for water supply projects. The remaining 2.5% consists of general construction projects.

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 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 (SB 202) 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.

The number and value of prevailing wage projects has risen dramatically in just two years. DLLR advises that its prevailing wage unit currently monitors more than 500 projects, compared with 187 in fiscal 2011. The total value of those projects has also increased, from $3.1 billion in fiscal 2011 to more than $4.1 billion currently, which includes projects procured by local governments. In fiscal 2012, the unit investigated 535 project sites for prevailing wage compliance, recovered $755,472 in unpaid wages on behalf of laborers, and collected $218,525 in liquidated damages on behalf of the State and local governments.

Four Maryland jurisdictions – Allegany, 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, including school construction.

Economic Effects of Prevailing Wages

For this bill and recent prior versions of other prevailing wage bills, DLS has conducted an extensive review of research on the effect of prevailing wage laws on the cost of public works contracts and found inconsistent 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. Therefore, research findings related to the effect of the prevailing wage on project costs are inconsistent and often inconclusive.

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%, but those studies were hampered by the control group challenge identified above.

Recent empirical data from the Public School Construction Program 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. Recent bid solicitations for three new or replacement schools in Howard and Washington counties used this approach. Based on the lowest submitted prevailing wage bids, the use of prevailing wages increased the bids by 6.6%, 8.2%, and 8.7%, respectively. Although the sample is not large enough to draw any firm conclusions, it is possible that the gap between market and prevailing wages is lower in more urban areas of the State, where there is greater competition for construction projects.

These empirical findings have been countered over the past 10 years by studies that have found no statistically significant effect of prevailing wages on contract costs. Among the possible reasons cited in these studies for the absence of a cost effect include:

- 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 is that labor costs, including benefits and payroll taxes, represent between 20% and 30% of construction costs. Therefore, a 10% gap between prevailing wages and market wages would increase total contract costs by about 2.5%. That is consistent with the findings of some of the empirical studies that have been conducted, but as noted above, recent 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, and in some cases they may be negligible.

State Fiscal Effect: The bill results in a substantial increase in the number of prevailing wage projects subject to enforcement oversight by DLLR. WSSC advises that wastewater treatment projects, one of the two largest components of its capital expenditures, already comply with prevailing wage requirements because they typically meet the 50% State funding threshold in current law. Water and sewer main replacement projects are the other largest capital component. WSSC cannot provide a reliable estimate of the number of affected projects, but given the magnitude of its capital budget, it is expected that a significant number of future projects are affected. DLLR estimates that it may be as many as 120 projects in the coming years.

As noted above, DLLR has experienced nearly a three-fold increase in the number of prevailing wage projects it oversees without a commensurate increase in staff. Therefore, it cannot absorb any further increase in the number of prevailing wage projects without an increase in staffing. General fund expenditures increase by $92,875 in fiscal 2014, which accounts for the bill's October 1, 2013 effective date. This estimate reflects the cost of hiring two wage and hour investigators to enforce WSSC compliance with prevailing wage requirements. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Positions	2
Salaries and Fringe Benefits	$76,182
Operating Expenses	16,693
Total FY 2014 State Expenditures	**$92,875**

Future year expenditures reflect full salaries with annual increases and employee turnover as well as annual increases in ongoing operating expenses and the termination of one-time costs.

Local Revenue Effect: To the extent that WSSC contractors do not comply with prevailing wage requirements, they are subject to payment of liquidated damages under the prevailing wage law. Although DLLR assesses the payments based on its findings of noncompliance, the damages are paid to WSSC.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Department of General Services; Washington Suburban Sanitary Commission; Department of Labor, Licensing, and Regulation; Department of Legislative Services

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