SB 232

Department of Legislative Services

Maryland General Assembly
2020 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 232 (Senator Benson, *et al.*)
Finance

Procurement - Prevailing Wage - Applicability

This bill requires non-State public work projects, other than public schools, that are funded in whole or in part with State funds (instead of with at least 50% in State funds) to pay workers the prevailing wage, subject to existing limitations and exemptions.

Fiscal Summary

State Effect: Special fund revenues for the Maryland Department of Labor (MDL) increase by $40,500 in FY 2021 and then annually thereafter by $54,000. General fund expenditures by MDL increase by $49,700 in FY 2021 for enforcement; out-year costs reflect annualization and ongoing costs for enforcement.

(in dollars)	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
SF Revenue	$40,500	$54,000	$54,000	$54,000	$54,000
GF Expenditure	$49,700	$57,800	$59,000	$60,900	$62,900
Net Effect	($9,200)	($3,800)	($5,000)	($6,900)	($8,900)

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

Local Effect: Local capital projects that receive State funding but were not previously required to pay prevailing wages must now do so. As a result, total project costs likely increase by between 2% and 5%. Any such increase likely does not affect total local capital expenditures but may result in fewer local projects being funded each year. Contractors on some local projects may also be required to either participate in an apprenticeship training program or make specified payments. **This bill may impose a mandate on a unit of local government.**

Small Business Effect: Potential meaningful.

Analysis

Current Law: For a complete description of the State's prevailing wage requirements, and their effects on the cost of public work projects, please see the **Appendix – Maryland's Prevailing Wage Law.**

State Apprenticeship Training Fund and POWER Act

Chapter 687 of 2009 established the State Apprenticeship Training Fund (SATF) as a special, nonlapsing fund, and requires contractors and some subcontractors on public work contracts that *are* subject to the prevailing wage law to either (1) participate in an apprenticeship training program; (2) make payments to a registered apprenticeship program or to an organization that operates registered programs for the purpose of supporting the programs; or (3) make specified payments to the fund. The fund's revenues consist entirely of payments made by contractors and penalties collected due to violations of the statutory provisions.

Chapter 782 of 2017 – the Providing our Workers Education and Readiness (POWER) Act – expanded these requirements to encompass specified construction projects that are *not* subject to the prevailing wage requirements. Specifically, the POWER Act applies to construction contracts valued at $500,000 or more for any construction projects that receive at least $1.0 million in funding from the State's capital budget.

Monies from SATF may be used only to promote preapprenticeship programs and other workforce development programs in the State's public secondary schools and community colleges and to cover any costs associated with carrying out Subtitles 6 and 6A of Title 17 of the State Finance and Procurement Article (Chapters 687 and 782, respectively). The programs should prepare students to enter apprenticeship training programs.

Background: The Department of General Service's (DGS) Office of Capital Grants and Loans oversees local, private, and nonprofit grantees that receive grants from the State to partially fund capital projects. Currently, there are almost 1,700 active projects, with about 300 new projects added each fiscal year. As most grant recipients are required to provide matching funds as a condition of obtaining a grant from the State, and many obtain funding from other sources, very few of those projects currently reach the 50% State funding threshold in current law for application of the prevailing wage law. Many grant projects also do not reach the $500,000 contract value threshold. Previously, DGS has advised that, while some grantees are large institutions (*e.g.,* hospitals) that require minimal assistance and oversight, many grantees are small nonprofit organizations with limited or no experience managing capital projects and, therefore, require substantial assistance and oversight from DGS.

The Maryland Department of Labor (MDL) advises that SATF collects an average of $22,500 per month, or $270,000 per year, combined from projects under Chapter 687 and the POWER Act. As of February 2020, the fund had a balance of $887,521.

State Revenues: Projects affected by the bill do not currently pay prevailing wages and, therefore, are subject to the POWER Act *if* they receive at least $1.0 million from the State's capital budget. Based on data provided by DGS, few grant recipients reach that threshold (for instance, in fiscal 2019, 40 out of 312 grantees reached the threshold; in prior years, there were fewer such projects), so most grantees are not subject to the POWER Act requirements. This analysis assumes that current active projects are not affected by the bill because they already have signed contracts. It further assumes, however, that under the bill, 300 *new* capital grant recipients may be subject to prevailing wage requirements each year if they reach the $500,000 contract value threshold. This analysis also assumes that 25% of those projects do not meet the threshold, leaving 225 projects that become subject to the prevailing wage requirements.

Under current law, covered projects can either participate in an apprenticeship training program, contribute directly to a program, or pay SATF. Thus, not all contractors pay the fund. This analysis assumes that payments to the fund are made proportionally to current levels. Currently, contractors on 1,120 prevailing wage projects make payments totaling $270,000 annually, so it is anticipated that 225 new projects (20% of the current total) generate an additional $54,000 in revenues for SATF annually, which is 20% of the current annual payments made to the fund. Accounting for the bill's October 1, 2020 effective date, revenues in fiscal 2021 are $40,500.

State Expenditures: The bill does not apply to State capital construction projects, which are already subject to prevailing wage requirements if they meet the $500,000 contract value threshold. Thus, the bill's effects are to require non-State capital projects, except public schools, that previously did not meet the 50% State funding threshold to pay prevailing wages. As noted above, this analysis assumes that 225 projects become subject to prevailing wage requirements.

MDL currently enforces prevailing wage requirements for 1,120 projects with five investigators, or roughly one investigator for every 225 projects. Therefore, MDL needs one additional wage and hour investigator to enforce prevailing wage requirements for the anticipated 225 additional projects. Under the assumption that SATF cannot be used for prevailing wage enforcement (which falls under Subtitle 2 of Title 17 of the State Finance and Procurement Article), general fund expenditures increase by $49,651 in fiscal 2021, which accounts for the bill's October 1, 2020 effective date. This estimate reflects the cost of hiring one wage and hour investigator to enforce prevailing wage requirements for the additional projects. It includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses.

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Salary and Fringe Benefits	$41,860
Operating Expenses	7,791
Total FY 2021 State Expenditures	**$49,651**

Future year expenditures reflect a full salary with annual increases and employee turnover and ongoing operating expenses.

This analysis assumes DGS can handle additional inquiries and technical assistance for nonprofit organizations affected by the bill with existing resources. To the extent the volume of inquiries is greater than anticipated, additional staffing may be required.

As SATF has additional revenues available, special fund expenditures may also increase minimally to promote preapprenticeship programs and other workforce development programs, but any such expenditures are not required by this bill.

Small Business Effect: Contractors on construction projects that receive State funds but that are not currently subject to the prevailing wage must pay prevailing wages. In addition, many of these same contractors must either participate in an apprenticeship training program or make payments to a program or SATF. Contractors likely pass on these costs to project sponsors, thereby increasing project costs.

Additional Information

Prior Introductions: None.

Designated Cross File: HB 582 (Delegate Valderrama, *et al.*) - Economic Matters.

Information Source(s): Anne Arundel, Baltimore, Charles, Frederick, and Montgomery counties; Maryland Association of Counties; City of Havre de Grace; Maryland Municipal League; Department of General Services; Maryland Department of Labor; Department of Legislative Services

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mr/ljm

Analysis by: Michael C. Rubenstein

Direct Inquiries to:
(410) 946-5510
(301) 970-5510

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;
- an elementary or secondary school for which at least 25% of the money used for construction is State money;
- any other public work for which at least 50% 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 $500,000 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 or (2) specified construction projects carried out by public service companies under order of the Public Service Commission.

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, Morgan State University, St. Mary's College of Maryland, and the Maryland Stadium Authority are all exempt from the prevailing wage law.

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, making almost all public school construction projects in the State required to pay the prevailing wage, subject to the $500,000 contract value threshold.

The number of prevailing wage projects has risen dramatically in recent years. MDL advises that, during fiscal 2019, its prevailing wage unit monitored 1,120 projects, up from 958 in fiscal 2018, and significantly up from 496 in fiscal 2014. To accommodate the increase in projects, the number of prevailing wage investigators increased in fiscal 2016 from three to six; there are currently five investigators.

Five Maryland jurisdictions – Allegany, 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.

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."

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 then 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 and data quality challenges identified above.

More recent empirical data from several counties 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. 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.

Over the past 10 to 15 years, multiple large-scale studies have found no statistically significant effect of prevailing wages on contract costs. As with the earlier studies that found a project cost effect, control group and data quality issues may have also affected these studies' findings, but the studies themselves cited the following possible explanations for the absence of a cost effect:

- 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, and which is supported by the U.S. Bureau of Labor Statistics, is that labor costs represent between 20% and 30% of construction costs. Therefore, a 10% gap between prevailing wages and market wages could theoretically increase total contract costs by about 2.5%, and a 40% gap in wages could increase total contract costs by about 10%. That is consistent with the findings of some of the empirical studies that have been conducted, but as noted above, more recent empirical 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, with some projects exhibiting higher cost differences and others experiencing negligible differences.