



Senate Fiscal Agency
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BILL ANALYSIS



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Senate Bill 1 (as passed by the Senate)
Senate Bill 2 (Substitute S-1 as passed by the Senate)
Senate Bill 3 (Substitute S-1 as passed by the Senate)
Sponsor: Senator Arlan Meekhof (S.B. 1)
 Senator Peter MacGregor (S.B. 2)
 Senator Dave Robertson (S.B. 3)
Committee: Michigan Competitiveness

Date Completed: 8-27-15

RATIONALE

Under Michigan's prevailing wage law, contracts for construction projects that are financed or financially supported by the State must require the contractor to pay construction workers wages and fringe benefits that are not less than the wages and benefits prevailing in the locality where the work is to be performed. The prevailing wages and benefits must be determined by the Department of Licensing and Regulatory Affairs based on the rates under collective bargaining agreements that cover the locations of the projects. For example, if the State contracted with a construction company to build a prison in the City of Lansing, or the State acted as surety for the payment of bonds issued by the Lansing School District to pay for school building renovations in the city, the contractor would have to pay its construction workers at least the wages and benefits determined to be prevailing in that area, based on local collective bargaining agreements. Except during a period of two and a half years in the 1990s, the prevailing wage law has been in effect since 1966.¹ Michigan's law is generally patterned after the Federal prevailing wage law, also known as the Davis-Bacon Act, whose purposes are described as, "to protect the employees of Government contractors from substandard wages and to promote the hiring of local labor rather than cheap labor from distant sources".² Many people believe, however, that Michigan's law is unnecessary and inflates construction costs, which are ultimately paid by taxpayers. Thus, it has been suggested that the law should be repealed.

CONTENT

Senate Bill 3 (S-1) would repeal Public Act 166 of 1965, commonly known as the prevailing wage law. The bill also would appropriate \$75,000 from the General Fund in fiscal year 2015-16 to the Department of Licensing and Regulatory Affairs for it to implement and disseminate information about the repeal.

Senate Bills 1 and 2 (S-1) would amend the Revised School Code and the Economic Development Corporations Act, respectively, to delete provisions related to the prevailing wage law.

Senate Bills 1 and 2 (S-1) are tie-barred to Senate Bill 3. A more detailed description of Senate Bills 1 and 2 (S-1) follows. For detail about the language of the prevailing wage law, please see the **BACKGROUND** section below.

¹ In November 1994, the U.S. District Court for the Eastern District of Michigan held that the State's prevailing wage law was preempted by a Federal law, the Employee Retirement Income Security Act. This decision was overturned in June 1997 by the U.S. Court of Appeals, Sixth Circuit (*Associated Builders and Contractors Saginaw Valley Area Chapter v. W Perry*, 115 F3d 386).

² Michigan Supreme Court opinion (*Western Michigan University Board of Control v. State of Michigan*, 455 Mich 531) quoting the U.S. Court of Appeals, Fifth Circuit (*North Georgia Building & Construction Trades Council v. Goldschmidt*, 621 F2d 697).

Senate Bill 1

The Revised School Code requires a public school academy, urban high school academy, school of excellence, and strict discipline academy to comply with all applicable laws, including statutes listed in the Code. The bill would delete the prevailing wage law from those listed.

Senate Bill 2 (S-1)

The Economic Development Corporations Act requires an economic development corporation to prepare a project plan and requires the plan to contain certain information, including a statement of the proposed method of financing the project. The bill would delete a requirement that the statement indicate the payment to construction workers of the prevailing wage and fringe benefit rates for the same or similar work in the locality where the work is to be performed. The bill also would delete a requirement that those rates be determined under the prevailing wage law.

In addition, the Act provides that a corporation may rely conclusively upon the required statement as to compliance with the payment of prevailing wage and fringe benefit rates, and any contracts, bonds, or notes of a corporation entered into or issued upon reliance on any statement may not be voided due to failure to comply with the requirements described above. The bill would delete that provision.

MCL 308.503 et al. (S.B. 1)
125.1608 (S.B. 2)
408.551-408.558 (S.B. 3)

BACKGROUND

Requirement to Pay Prevailing Wage

Public Act 166 of 1965, the prevailing wage law, contains the following language:

Every contract executed between a contracting agent and a successful bidder as contractor and entered into pursuant to advertisement and invitation to bid for a state project which requires or involves the employment of construction mechanics, other than those subject to the jurisdiction of the state civil service commission, and which is sponsored or financed in whole or in part by the state shall contain an express term that the rates of wages and fringe benefits to be paid to each class of mechanics by the bidder and all of his subcontractors, shall be not less than the wage and fringe benefit rates prevailing in the locality in which the work is to be performed.

In other words, to be subject to the Act, a project must meet all of the following criteria:

- Be with a "contracting agent".
- Be entered into after advertisement or invitation to bid.
- Be a "state project".
- Require the employment of "construction mechanics".
- Be entirely or partly sponsored or financed by the State.

The Act defines "contracting agent" as any officer, school board, board or commission of the State, or a State institution supported in whole or in part by State funds, authorized to enter into a contract for a State project or to perform a State project by the direct employment of labor.

According to the "Act 166 Policy Manual" of the Wage and Hour Division in the Department of Licensing and Regulatory Affairs, "Michigan's prevailing wage law covers State, public schools, charter schools, community colleges, state colleges and university projects, paid for by state funds

or state backed bonds."³ The manual also notes that the Act does not cover construction projects initiated by cities, townships, or counties, or by other entities not defined in the Act as "contracting agents".⁴

Public Act 166 defines "state project" as new construction, alteration, repair, installation, painting, decorating, completion, demolition, conditioning, reconditioning, or improvement of public buildings, schools, works, bridges, highways, or roads authorized by a contracting agent.

"Construction mechanic" means a skilled or unskilled mechanic, laborer, worker, assistant, or apprentice working on a State project. The term does not include executive, administrative, professional, office, or custodial employees.

"Locality" means the county, city, village, township, or school district in which the physical work on a State project is to be performed.

Determination of Prevailing Rates

Before a contracting agent advertises for bids on a State project, the agent must have the Department of Licensing and Regulatory Affairs (LARA) determine the prevailing rates of wages and fringe benefits for all classes of construction mechanics called for by the contract.⁵ A contracting agent's request must include the rate schedule or schedules required and any additional specific classifications the agent needs that are not included.

The contracting agent must include the schedule of prevailing rates in the specifications for the work to be performed. If a contract is not awarded or construction is not begun within 90 days after LARA's determination, the Department must make a redetermination before the contract is awarded.

The Department is required to establish prevailing wages and fringe benefits "at the same rate that prevails on projects of a similar character in the locality under collective agreements or understandings between bona fide organizations of construction mechanics and their employers". That is, prevailing rates are compiled from the rates contained in collectively bargained agreements that cover the locations of the State projects. Typically, the prevailing rates that apply are the rates for the county where a project is located. For in some cases, however, a prevailing rate for a particular classification might apply only in certain subdivisions of a county, such as specific townships.

Exemption

The Act does not apply to contracts on State projects that require the payment of prevailing wages as determined by the U.S. Secretary of Labor under the Davis-Bacon Act, or that contain minimum wage schedules that are the same as prevailing wages in the locality as determined by collective bargaining agreements or understandings between bona fide organizations of construction mechanics and their employers.

³ In *Western Michigan University Board of Control v. State of Michigan*, the Michigan Supreme Court held that a State university is considered a contracting agent under the prevailing wage law. The "Act 166 Policy Manual" cites this decision and states, "Projects of public Universities and colleges are generally considered state projects unless the documentation shows that the source of funding is federal funds."

⁴ The manual also points out that political subdivisions or governmental units that are not contracting agents may have their own prevailing wage requirements, but those requirements are not subject to Public Act 166.

⁵ The Act requires the rates to be determined by the "Commissioner", which originally referred to a former Department of Labor. As a result of transfers made under several Executive Orders, the Wage and Hour Division in LARA currently is responsible for determining prevailing rates.

Other Provisions

Public Act 166 requires every contractor and subcontractor to conspicuously post on the construction site a copy of all prevailing wages and fringe benefit rates prescribed in a contract. Every contractor and subcontractor also must keep an accurate record of the name and occupation of, and the actual wages and benefits paid to, each construction mechanic employed by the contractor or subcontractor in connection with the contract.

A contracting agent, by giving written notice to the contractor and its sureties known to the agent, may terminate the contractor's right to proceed under the part of the contract for which less than the prevailing wage and benefits have been or will be paid. The contracting agent may complete the contract by an agreement with another contractor or otherwise, and the original contractor and its sureties are liable for any excess cost that results.

The Act makes it a misdemeanor to violate the Act but does not prescribe a penalty. (Under the Michigan Penal Code, a misdemeanor for which a penalty is not prescribed is punishable by imprisonment for up to 90 days or a maximum fine of \$500, or both.)

Complaints

According to the Department, a person who has not been paid the prevailing rate on a State project may file a complaint with the Wage and Hour Division within LARA. The Department will investigate and attempt to resolve the dispute informally. If voluntary resolution is not successful, the complaint will be referred to the prosecuting attorney for enforcement action.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Because local prevailing wages are based on union contracts, which generally require the payment of above-average wages, the prevailing wage law drives up the costs of public construction projects. When a contractor is required to pay high wages and benefits, those costs are reflected in the amount paid by the State or other governmental entity entering into the contract. This means that taxpayers pay more for the construction and renovation of public buildings than those in the private sector have to pay for comparable work. The higher cost of a project also increases the cost of financing, which is passed on to the taxpayers as well. Repealing the law would mean that contracting by the State, school districts, and other bodies that have State backing would be consistent with what is occurring in the rest of the construction industry.

In addition to increasing costs for Michigan taxpayers, the law puts this State at a competitive disadvantage. Reportedly, 44 other states either do not have a prevailing wage law or have one that is not as rigid as Michigan's, and Michigan is one of only six states in which the prevailing wage is based entirely on union contracts. Since less than one quarter of the construction workers in the State are unionized, this disproportionately and unfairly increases labor costs.

Furthermore, the law generates a tremendous amount of administrative work for contractors bidding on State projects, who must determine which wage classifications apply to a particular job. When seeking bids, a contracting agent will request the prevailing wage schedule for the county and include the schedule in the contract specifications, and a contractor bidding on the project will have to base its bid on the applicable classifications. In its 2015 prevailing wage rate list, the Wage and Hour Division in LARA lists 463 classifications that are categorized by type of work; the category "bricklayer", for example includes 21 separate classifications, and the category "electrician" includes 35 separate classifications. The applicable wage for a classification, however, may depend on the day of the week worked; the numbers of hours put in; whether the wage is straight hourly, time-and-a-half, or double time; whether there is a separate rate for holiday pay; whether a makeup day is allowed for bad weather; whether the project is a subdivision of a county with its own prevailing rate; and whether the worker is an apprentice and, if so, the number of

months or years he or she has worked. Since a separate list is created for each county, and each county might contain multiple subdivisions, considering all of the potential variations for the different classifications, it is possible to count over 300,000 classifications statewide, according to the Associated Builders and Contractors of Michigan.

Identifying the classifications that apply to a project is not only difficult but also costly, which contributes to the costs ultimately passed on to the taxpayers. In addition, while the process is complex and demanding for all contractors, it is especially burdensome to nonunion contractors, who might not understand the nuances of union work classifications. It also may prevent some small and minority-owned contractors from attempting to bid, if they do not have the resources to meet the demands of the law.

Repealing the law would open give more contractors an opportunity to compete on State construction contracts, and increased competitiveness would allow the State to seek out the best deal for a project. While the lowest-cost bidder would not necessarily get the contract, the State and other contracting agents would have more choices. To the extent that lower labor costs reduced the overall costs of construction contracts, tax dollars could be used to meet other needs of Michigan residents.

In addition, repealing the law would save the State the administrative costs of determining what wage rates prevail in a region, as well as the costs of enforcing the law and resolving complaints.

Response: Reportedly, states without a prevailing wage law do not have lower bids for construction projects. Rather, they have higher profits for contractors.

Supporting Argument

In November 2013, Anderson Economic Group, LLC, (AEG) issued a report estimating that in each year from 2002 to 2011, the prevailing wage law created nearly \$225.0 million in added costs for the construction of public K-12 and higher education facilities in Michigan.⁶ This was based on estimates that nearly \$3.0 billion in education construction expenditures are subject to the prevailing wage law each year, and of that amount, the cost of labor accounts for nearly \$900.0 million. The AEG analysis also estimated that Michigan's prevailing wage rates are approximately 25% higher than the private market. According to the report, if the additional amount resulting from the prevailing wage had not been spent, K-12 schools would have saved \$137.0 million, while community colleges and institutions of higher education would have saved \$87.0 million, each year between 2002 and 2011.

Earlier reports by the Mackinac Center for Public Policy also concluded that the prevailing wage law increases labor costs, thereby increasing the costs of government construction contracts. In September 1999, the Mackinac Center reported on an analysis of construction costs and employment rates for then-recent periods with and without a prevailing wage law.⁷ Among other things, the study compared the creation of construction jobs during the 30 months after the law was invalidated by the Federal court (December 1994 to June 1997) and the preceding 30-month period when the law was in effect. The study found that 78.61 construction jobs were created for each 1,000-job increase in total employment between June 1992 and December 1994. However, "In the two-and-a-half years without an operative prevailing wage, Michigan employers created 116.27 new construction jobs per 1,000 total new jobs, an increase of nearly 48 percent." In addition, "During the 30-month period of no prevailing wages in Michigan, there is evidence of numerous government construction projects being carried out with significant savings arising from the use of non-union scale labor."

⁶ "The Impact of Michigan's Prevailing Wage Law on Education Construction Expenditures", Anderson Economic Group, LLC, by Alex L. Rosean, Senior Consultant, Commissioned by Associated Builders and Contractors of Michigan, 11-13-2013.

⁷ "Michigan's Prevailing Wage Law and Its Effects on Government Spending and Construction Employment", Mackinac Center for Public Policy, by Richard Vedder, Ph.D., September 1999.

The Mackinac Center issued another report on the prevailing wage in 2007.⁸ This report came to the following conclusion: "The prevailing wage law forces the payment of union wages on state construction projects despite the fact that union workers made up just 22.1 percent of the construction work force in Michigan in 2006. In the process, the law provides a boost in compensation of 40 percent to 60 percent to construction workers who already receive wages well above the average for workers in this state. This cost is ultimately passed on to Michigan taxpayers, who lose \$232 million annually -- a conservative estimate calculated in 2002 dollars -- without any discernable benefit for the vast majority of Michiganians."

Response: Although it is possible to calculate the difference between union wages and nonunion wages, and to conclude that the amount of this difference is added to the costs of a construction contract subject to the prevailing wage law, it cannot be assumed that the cost of the project would be reduced by that amount if union wages were not paid or that taxpayers would experience savings if a lower bid could be accepted. While a low bid might produce temporary savings, ultimately costs are likely to be driven up by a number of factors, especially if the bid is artificially low. For example, change orders probably occur during the course of any construction project but are more prevalent when a bid is low. Expensive repairs might be needed if the quality of the work is shoddy, and liability might be an issue if safety standards are not met. Any of these factors may lead to costly litigation, as well.

Opposing Argument

The prevailing wage law benefits the public, workers, the economy, and the construction industry in a number of ways. First, everyone benefits from increased safety when a project uses highly trained skilled labor. The workers themselves risk fewer accidents on the job site, and members of the public are exposed to fewer hazards when construction is not substandard. It simply is unwise to hire low-paid, low-skilled workers to build schools, bridges, office buildings, hospitals, and other public facilities.

The prevailing wage law supports training through union apprenticeship programs and otherwise, attracts young people to the construction trades, and keeps trained workers in the State. Repealing the law would have the opposite effect: driving skilled workers away and opening the door to out-of-State contractors who would underbid Michigan companies and replace Michigan workers with lower-paid, less-skilled, and likely transient laborers. By ensuring that Michigan continues to have a well trained, highly skilled construction labor force, the law helps the State remain competitive.

In addition, workers who receive decent wages provide stability in the labor market and have more disposable income. Higher wages also are associated with increased productivity, which benefits not only the employers but also the taxpayers who are paying for the State-supported projects. When local construction firms are not underbid by out-of-State contractors, they are able to expand their operations and invest in their communities. Higher earnings for both workers and businesses boost other local enterprises, such as restaurants, real estate agencies, retailers, and accounting firms.

Response: With respect to claims of increased safety due to the prevailing wage law, the same construction codes apply whether a project is subject to the law or not, so safety should not be affected. Also, training can be provided through programs unrelated to unions, such as community college programs and on-the-job training.

Opposing Argument

A recent study by the Midwest Economic Policy Institute examined the potential impact of repealing Michigan's prevailing wage law.⁹ A report published in June 2015 contains the following conclusion: "Ultimately, the prevailing wage for publicly-financed construction projects is a positive economic development tool providing substantial benefits to workers, contractors, families, and the overall economy. Weakening or repealing Michigan's prevailing wage law will not reduce the cost of public construction and is not in the best interest of taxpayers. Instead, repeal would result in job losses

⁸ "The Effects of Michigan's Prevailing Wage Law", Mackinac Center for Public Policy, by Paul Kersey, 2007.

⁹ "The Cost of Repealing Michigan's Prevailing Wage Policy: Impacts on Total Construction Costs and Economic Activity", Midwest Economic Policy Institute, by Kevin Duncan, Ph.D., Alex Lantsberg, MCP, AICP, and Frank Manzo IV, MPP, 6-25-2015.

and would reduce tax revenues in Michigan. Prevailing wage supports a dynamic, 'high road' economy that promotes worker productivity and boosts economic activity."

According to the report, if the law were repealed, "An estimated \$673 in construction value would be completed by out-of-state contractors. This would result in a significant decrease in revenue for in-state businesses. Construction worker wages and benefits would fall by \$962 million but materials and fuels costs would rise by \$781 million. In addition, proprietor (or contractor) income would increase by \$223 million -- indicating a transfer of income from workers to owners.

"Ultimately, these impacts would result in 11,320 jobs lost and a \$1.70 billion reduction in economic activity across Michigan, representing a 0.38 percent loss of state GDP if prevailing wage is repealed." Also, according to the report, State and local tax revenue would fall by more than \$28.0 million per year.

Response: The interests of the State's residents are served when the government is able to obtain goods and services for the lowest reasonable cost, not when tax revenue is maximized.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bills would have an indeterminate, but likely positive, fiscal impact on the State and local units of government. The bills would eliminate the requirement that workers on State-funded construction projects be paid wages and fringe benefits that meet or exceed levels established by the Wage and Hour Division within the Department of Licensing and Regulatory Affairs. Affected construction projects include State buildings, universities, roads, and public schools. Additionally, projects undertaken by economic development corporations, public school academies, and certain other types of schools are currently subject to these requirements as well. The bills would remove the prevailing wage requirements, and could produce potential savings on these types of projects. The amount of potential savings is indeterminate and dependent on the wages ultimately paid to workers who otherwise would have been paid at the prevailing wage rates. Lack of available data makes it difficult to estimate with any certainty how much would be saved if the bills were enacted. Factors that could affect the amount of actual savings include the degree of competition among contractors in bidding on projects and the strength of the labor market.

It should be noted that projects funded with Federal funds still would be subject to the Federal Davis-Bacon Act, which establishes prevailing wages for construction projects over \$2,000 that are funded wholly or in part with Federal funds. Prevailing wages under the Davis-Bacon Act are fairly similar to Michigan's prevailing wages, so it is unlikely that the bills would produce significant savings for State or local projects that receive Federal funds. The largest category of projects that would continue to be affected by prevailing wages due to the use of Federal funds is construction and maintenance of State trunkline highways; most of these projects receive Federal funds.

In addition, Senate Bill 3 (S-1) would appropriate \$75,000 from the General Fund to LARA for the dissemination of information related to the repeal of the prevailing wage law.

Fiscal Analyst: Joe Carrasco
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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.