



THE CITY OF SAN DIEGO
MANAGER'S REPORT

DATE ISSUED: May 30, 2003 REPORT NO. 03-111

ATTENTION: Rules, Finance and Intergovernmental Relations Committee
Agenda of June 4, 2003

SUBJECT: Prevailing Wage Requirements For City Projects

SUMMARY:

Issue -

1. Should the City include prevailing wage requirements in the City's municipal affair projects?
2. Should staff attend the Department of Industrial Relations meeting of June 6, 2003 to testify against applying prevailing wages to off-site fabrication?

Manager's Recommendations -

1. Do not include prevailing wage requirements in the City's municipal affair projects.
2. Direct staff to attend the Department of Industrial Relations meeting of June 6, 2003 to testify against applying prevailing wages to off-site fabrication.

Other Recommendations - None.

Fiscal Impact - None with this action. However, including prevailing wage requirements in the City's municipal affair construction projects would likely increase the capital costs of projects.

BACKGROUND

In general, prevailing wages are required for City construction projects only when mandated by the use of state or federal funds or when a project is otherwise a statewide concern. Prevailing wages are not required for projects that are considered to be a municipal affair. However, the City may include prevailing wage specifications in its public works municipal affair contracts if it

is determined, by the Mayor and City Council on a project-by-project basis that the specification is consistent with the San Diego Charter.

Attachment (1) lists all City projects that have been advertised for construction during the last two years including whether or not prevailing wages were required and the funding source. It indicates that over the past two years 47% (35% in dollar value) of all City contracts required a prevailing wage specification due to the requirements of federal and/or state funding sources.

On April 21, 2003, the City Council approved the plans and specifications and authorized award of Miramar Water Treatment Plan Contract A, a municipal affair project, with the requirement that a prevailing wage specification be included in the contract package. In addition, the Council directed staff to analyze the impact of including prevailing wages requirements in all City projects and report back to the Rules Committee with findings and potential cost impacts.

DISCUSSION

Research (Nationwide)

Of the fifty states, thirty-two have prevailing wage statutes. The threshold amounts for public works contract coverage in those states with prevailing wage requirements range from \$0 to \$500,000. Of the eighteen that do not have prevailing wage legislation, ten states have either repealed prior legislation or their legislation was invalidated by court decision.

Numerous jurisdictional studies have been conducted in the attempt to determine if prevailing wage statutes result in increased public works construction costs. A Michigan study asserted that "prevailing wage" law increased construction costs by ten percent. A five percent to fifteen percent increase as a result of "prevailing wage" was estimated in studies using data provided by several states. The findings of these studies range from "prevailing wage laws have not statistically significant effect on construction costs" to estimates "that the Davis-Bacon Act increased construction costs of public projects by 26 percent". One study's statistical analysis indicates that there is no increase in cost as a result of "prevailing wage," but the real cost driver is the difference in the requirements for prosecuting public and private projects.

Typically, the intent of prevailing wage laws is to provide benefits such as health coverage, maintain community wage standards, support local economic stability and to protect the taxpayers from sub-standard labor. It is sometimes believed that by setting clear parameters contractors would bid on public projects on the basis of skill and efficiency. However, for the past few decades, these laws have been under scrutiny for several reasons, including fraudulent wage reporting to artificially inflate set prevailing wage rates, the purported unfairness to small businesses, and the claim of bias toward unionized companies. As mentioned above, some states and cities have repealed their local prevailing wage laws, with conflicting reports stating the benefits and losses. After reviewing fifty articles on this subject (see Attachment 3), it is very obvious that the debate is ongoing, and that studies exist which support either requiring prevailing

wages or not requiring prevailing wages.

Citywide Construction Cost Impact

Requiring prevailing wages on all City construction contracts could increase the capital cost of the projects mainly because prevailing wages are higher than at-will labor rates paid by the contractors. However, the rate of the increase depends on the type of project as it relates to the number of trades and skill levels required. For example, a typical pipeline or roadway project that requires a higher percent of unskilled labor (trades not in high demand) will be impacted more than a building project that requires a higher percent of skilled labor (trades in high demand).

City staff analyzed a few actual City projects to determine what the effect would be in the City of San Diego. We were able to perform this analysis by using actual certified payrolls, breaking down each project to a percentage of labor, equipment, and materials using the National Construction Estimator, and applying prevailing wage rates to those projects where they were not required and applying non-prevailing wage rates to projects in which prevailing wage rates were required. What was found is as follows:

- Labor costs on building projects increase 20% resulting in a total construction cost increase of approximately 7.5% when prevailing wages are required (Note: this would mean that a prevailing wage work force would need to be 20% more efficient to make up for these additional labor costs).
- On average, the increase in the construction cost of pipeline projects requiring payment of prevailing wages is as high as 17% as the labor costs increase 20% to 40% higher (depending on the wage rates used by individual non-prevailing wage contractors) than the non-prevailing wage pipeline projects.
- For road projects, the percentage increase for the total construction is approximately 16% due to prevailing wages as labor increases are 20-35%.

California and Local Laws

General prevailing wage requirements are found in the California Labor Code, 1770-1778, pertaining to "Public Works and Public Agencies." State law requires that prevailing wages be paid on certain public works projects. The courts have held that the state's prevailing wage law is a general law and does not apply to the public works municipal affair projects of a chartered city. As such, the City of San Diego is not required to include a contract specification for the payment of prevailing wage in its public works municipal affair project. However, the City Attorney has opined that the Charter does not necessarily prohibit the payment of prevailing wage on the City's public works municipal affair projects, but the City must do so only after a project-by-project review.

The City of San Diego is a charter City, and as such the City may not act in conflict with the

Charter. The Charter requires the City to competitively bid and award certain public works municipal affair projects to the lowest responsible and reliable bidder. A prevailing wage specification should not be in conflict with the Charter requirements if on a project-by-project basis there is evidence in the record that the specification serves to prevent the waste of public funds, will provide a cost benefit or will prove a corresponding economic benefit despite increasing the project costs. Additionally, the record should show that the specification is reasonably related to the quality, fitness, and capacity of a bidder to satisfactorily perform the proposed work. The City should not, however, include a prevailing wage specification in its public works municipal affair contracts unless the City Council rescinds or waives Resolution No. R-251555 that states that the City Council should not require prevailing wages on municipal affair projects.

The City uses federal or state funds imposing a prevailing wage requirement on its public works municipal affair projects when the use of those funds are necessary to construct the project. If a project is already fully funded and otherwise does not need state or federal funding, the City cannot add state or federal funding to the project for purposes of requiring prevailing wages. If the City desires to include a prevailing wage specification without conducting a project-by-project analysis as outlined above, the Charter must be amended.

Administrative Impacts

Requiring prevailing wages on all City public works would require additional staff in the City's Equal Opportunity Contracting (EOC) Program. A total of five additional staff with an estimated annual cost of \$358,670 will be required to adequately perform monitoring requirements. Attachment (2) includes the details on staffing and cost break down associated with additional monitoring requirements. These additional positions would likely charge their time to projects on which they work.

Impact By Program/Projects Type

As mentioned above, requiring prevailing wages on all City construction contracts would likely increase the capital costs of the projects. The rate of increase in cost depends on the type of project. This increase in most cases could result in the City's inability to complete some of the projects in the CIP program since less funds will be available for the same amount of work. An example, the water and sewer rate cases did not contemplate substantial increases in the CIP, thus the rates may have to be increased and/or new bonds issued sooner than expected in order to fund the programs mandated by the EPA and DHS. The following is the summary of the impacts by program/project type:

Water Projects

Requiring prevailing wages on CIP projects in the Water Program that are not currently budgeted for prevailing wages could increase the capital cost of those projects. This increase could result in the City's inability to complete the CIP program due to lack of available funds. If this occurs it may have to be included in the City's bond disclosure. This could also have credit implications

for the next series of bonds if the CIP program is not completed on schedule. See Manager's Report No. 03-072 dated April 16, 2003.

Application of prevailing wages would increase costs by approximately \$25 million over the next five years. Accommodating an increase in costs of this magnitude would require either adjustments to rates or the deferral of three or more projects, assuming an average cost per project of \$10 million. A project prioritization analysis would be required to determine the actual number of projects to be deferred, and a subsequent detailed financial analysis would be required to either validate the effectiveness of the deferrals and/or determine the magnitude of rate adjustments required.

Sewer Projects

The City must pay prevailing wages on projects associated with the Metropolitan portion of the City's wastewater system. The Metropolitan portion includes the Point Loma Wastewater Treatment Plant, the North City Water Reclamation Plant, the Metropolitan Biosolids Center, the South Bay Water Reclamation Plant, the North and South Metropolitan Interceptor Sewers, and other facilities. Improvements to these facilities always involve funds collected by the City from the Participating Agencies that use them. They may also include state and federal funds.

The City has not required prevailing wages on projects associated with the Municipal portion of the City's wastewater system, except in rare instances when state or federal funds are involved. The Municipal portion consists of sewer and pump stations that convey wastewater generated within the City. Improvements to the Municipal portion that are funded by City ratepayers are municipal affairs. However, if state or federal funds that require prevailing wages are used to help fund the improvements then a prevailing wage provision are a contract requirement.

If prevailing wages are implemented for improvements to the Municipal portion of the City's wastewater system, the total estimated cost increase is approximately \$16 million per year (over an approximately \$125 million annual program). An evaluation of the impact of prevailing wages on the Council approved rate increases of 7.5% annually through March 2005 is in process. The impact is likely to be substantial, assuming none of the anticipated improvements to the wastewater system are canceled or delayed.

Grants and FBA Funds

State and Federal Grants

There are approximately 20 projects scheduled for construction in FY 2004 that utilize State and Federal grants which require the payment of prevailing wages. As mandated with the use of state or federal funds, these projects already include the use of prevailing wages.

Facilities Benefit Assessment (FBA)

FBA funds are developer's "fair share fee" for infrastructure improvements. They are collected at the time building permits are issued in the applicable community and must be used for capital projects in the community where they are located. In FY 2004, there are approximately eleven transportation projects scheduled for construction. The estimated cost increase would be approximately \$4.4 million if prevailing wages were utilized.

As an example, in the North University City FBA, there are currently seven transportation projects and one library/park project scheduled for construction in FY 2004 none of which require prevailing wages. The cost increase of utilizing prevailing wages would be approximately \$4.5 million. The cost increases would need to be recovered by raising FBA fees, which could be significant depending how close to build-out the community is, or canceling or deferring projects.

Park and Recreation Projects

The Park and Recreation Department currently has approximately 166 programmed capital improvements projects from FY 2004 to FY 2014. Eighty (80) projects, or 48% of this capital program, currently are state and/or federal funded and require prevailing wages. Reflected in dollars, 30% of the \$316.5 million program requires prevailing wage (\$94 million). Below is a breakdown of the park projects by size and the spread of where prevailing wage applies in the program.

<u>Project Size</u>	<u>Prevailing Wage</u>	<u>Non-Prevailing Wage</u>
Up to \$500,000	62% - 43 projects	38% - 26 projects
\$500,000 to \$1 million	46% - 12 projects	54% - 14 projects
\$1 million to \$5 million	38% - 22 projects	62% - 36 projects
\$5 million and above	27% - 3 projects	73% - 10 projects

In evaluating the list of projects that represent those numbers, many of the projects up to \$1 million are funded by grants under the remaining Park Bond 2000, also referred to as Proposition 12. As the projects transition from \$1 million and above, Developer Impact Fees and Facilities Benefit Assessment Funds, i.e., local funding, becomes the primary source. It is in this area that prevailing wage will become a factor for the park program.

The park program ranges from relatively simple projects, such as, shade structures, tot-lot upgrades, hiking trails, dog off-leash areas, to medium sized projects such as, joint use areas, lighting projects, comfort stations, to the larger recreation and senior facilities, pools and new neighborhood and community parks. Therefore a specific percentage or average designated for general parks projects would be difficult. It is safe to say, that the recreation centers, senior centers and pools where "skilled labor" is in demand, would fall in line with those figures mentioned above at around 7.5% increases for total construction costs. The neighborhood and community park site improvements where there is turf and more basic amenities, where less "skilled labor" is needed, would be closer to the 17% mentioned for roadway projects.

The Park and Recreation Department also has approximately 171 projects that are not programmed as capital improvement projects. Many of these are community driven projects. In particular, adding prevailing wage to donation and Community Matching Funds Program projects may be simply impractical and undesirable to the community with the additional cost being difficult to absorb. Examples are: dog off-leash projects, re-paving parking lots, re-turfing fields, outdoor court resurfacing, poles and electrical fixtures for basketball courts, etc. It would be likely the Park and Recreation Department would lose some of these partnership opportunities.

Library/Fire Projects

The Library Program includes a combination of several funding sources. Prevailing wages are required for Otay Nestor, College Height/Rolando, Logan Heights, Ocean Beach, University Heights, and North Park since they are funded by CDBG/HUD 108. For the library projects that are not funded by CDBG/HUD 108, the total estimated construction cost increase is approximately \$6.8 million if the payment of prevailing wages is required. For the Fire Station upgrades the overall cost increase is approximately \$2.3 million if the payment of prevailing wages is required. See Attachment 4.

Housing Commission Projects

Typically Housing Commission projects do not pay prevailing wages on its projects. In recent years bills being considered by the State Senate have addressed whether or not to make this a requirement. While staff does not have the data available to perform an analysis of an impact, we believe it would be similar to public building projects such as libraries as the type of labor necessary to construct these projects is similar.

CONCEPT OF A "LIVEABLE WAGE"

As discussed in Attachment 2 to this report, prevailing wage requires an inordinate amount of paperwork, both on the contractor's part and City staff's part thus creating an additional cost of doing business for both parties. An alternative to the City of San Diego adopting federal prevailing wage (Davis-Bacon Act) or state prevailing wages (so-called "Little Davis Bacon") would be to create our own wage rates, accompanying components - such as benefits, and the rules that must be followed. Creating our own program (commonly called a Liveable Wage) would tailor the established wage rates for the different types of construction work to San Diego's economy, as opposed to the generic federal or state-wide rates that may or may not be adequate to our citizen's needs. Secondly, we would be able to establish a monitoring program that would likely be more efficient (in that we would not be monitoring that which is not essential to San Diego) as well tailored to what is important here.

According to the Center on Policy Initiatives, there are two common methods of calculating livable wage. One uses the federal poverty line and sets the wage to be what a full-time worker would need to support a family of four, which is \$18,100 or \$8.70 an hour. The other considers the local costs of living and calculates the wage that would cover a family needs budget. Based on the current Fair Market Rent of \$1095 for a two-bedroom apartment in San Diego County as

well as the cost of other basic needs such as food and transportation, The latter would likely be most appropriate if a liveable wage standard were developed.

OFF-SITE FABRICATION

On March 4, 2003 the State Department of Industrial Relations issued a determination that stated that, for project that required state prevailing wages, that prevailing wages should also be paid for off-site fabrication related to the project. Since that time the Acting Director has stayed the determination until a point in time that appeals could be heard. While this would certainly drastically exacerbate any cost increases due to prevailing wages, what is unknown at this time is 1) whether or not this would include off-site fabrication that takes place out of the state or country, and 2) how prevailing wages would be paid to trades for which a prevailing wages has not been determined. On June 6, 2003 the Department of Industrial Relations will be hosting a hearing in Golden Hall to receive comments from interested parties. City staff, with the Committee's authorization, could speak at this meeting and recommend opposing the determination.

ALTERNATIVE RECOMMENDATIONS:

1. Direct staff to conduct the research and prepare draft requirements for a localized "Liveable Wage", as described in the report.
2. Direct the City Attorney to prepare a Draft of a Charter Amendment such that prevailing wages would be allowable on all City projects.
3. Direct staff to bring forward draft findings for requiring prevailing wages on certain types of projects.

Respectfully submitted.

Frank Belock, Jr.
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Engineering and Capital Projects

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Senior Deputy City Manager

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Attachments:

1. Actual Costs and Funding for Public Work Contracts for FY 02 and FY 03 by MWWD and Engineering and Capital Projects, May 22, 2003
2. Prevailing Wage Impact Report: Staff Functions and Costs by EOCP, May 16, 2003
- 3a. Nationwide Research: Compilation of Articles For Prevailing Wage Laws by Water Department, May 19, 2003
- 3b. Nationwide Research: Compilation of Articles Against Prevailing Wage Laws by Water Department, May 19, 2003
4. Fire Stations and Library Program Prevailing Wage Impact by Engineering and Capital Projects, May 23, 2003

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