

Prequalification of Contractors: The Importance of Responsible Contracting on Public Works Projects

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Introduction

The construction of high quality public works projects is an essential component of an attractive quality of life and a competitive New York City economy. It is also imperative given the need for careful fiscal planning that the City take every step to ensure that all publicly-funded construction work is carried out by reputable and responsible contractors. Responsible contracting practices benefit not only the City and its taxpayers but contractors and workers as well. All responsible public works contractors need a level playing field. Through anti-competitive means, irresponsible contractors undercut sound business practices and artificially restrict opportunities for small, locally-based enterprises. All construction workers depend on the maintenance of good labor standards – compliance with prevailing wage and health and safety laws – that are jeopardized by irresponsible contractors.

While the importance of successful contracting to the City cannot be over-emphasized, as the New York State Organized Crime Task Force explains, a government enters the process of contracting with several crippling handicaps.¹ First, unlike a private entity that hires a contractor, the government must choose the lowest bidder among eligible contractors. Second, unlike a private entity, the government cannot simply say that it "does not like the job" a contractor did. The government must evaluate the quality of the work a contractor did objectively. But because in construction no two projects are the same, objective standards cannot be easily be defined. Wary of protracted battles with contractors, agencies often avoid them by giving contractors passing grades. In a 1998 report the Massachusetts Inspector General issued a report in which he stated: "Awarding authorities...are reportedly reluctant to provide unfavorable evaluations of contractors' performance on public contracts."² The result has been that unscrupulous contractors who plan to ask for change orders later on and to provide shoddy work through the use of unskilled workers often submit the lowest bids and impose great losses on the public.

Recognizing these handicaps, both the New York Organized Crime Task Force and the State of Massachusetts have concluded that the best solution is to **prequalify** contractors. According to the Organized Crime Task Force,

"the first step in combating fraud in public construction is to reform the contract letting system so that the City has greater control in selecting contractors for its multibillion dollar public works program. To accomplish this, the City needs **1) the authority to prequalify bidders**; 2) a strategy for increasing the size of the prequalified pool of contractors; 3) the ability and willingness to declare an

¹ Ronald Goldstock, "Corruption and Racketeering in the New York City Construction Industry," Final report to Governor Mario M Cuomo from the New York State Organized Crime Task Force," New York University Press: New York, 1991, Chapter 10.

² Massachusetts Office of the Inspector General Report, "Qualifying Contractors for Public Building Projects," August 1998. www.state.ma.us/ig/publ/ancx.htm.

unacceptable low bidder “not responsible;” 4) the authority to debar an incompetent, defaulting, or corrupt contractor from public contracting; and 5) the option to use letting procedures other than pure bidding.”³ (Emphasis added.)

In Massachusetts, according to its Inspector General, prequalification is mandatory because the state wants to assure the success of its public works programs:

“All contractors bidding on public building projects valued at more than \$25,000 must first be certified by the Division of Capital Asset Management (DCAM). Thousands of state and local agencies and governments across Massachusetts rely on DCAM to prequalify their contractors for public building contracts. **The success of building construction projects to provide essential public facilities such as public safety buildings, schools, libraries, and prisons depends heavily on DCAM’s ability to screen out unqualified contractors and to certify qualified contractors in a timely manner.**”⁴

Perhaps the best example of what prequalification can do for New York City comes from the cleanup of the World Trade Center site. That cleanup ended well ahead of schedule--estimates vary from 3 months to 1 year--and \$1 billion or more under budget.⁵ The process of selecting the contractors in this case involved what in effect was prequalification: because of the emergency the Department of Design and Construction was free to select contractors that it knew had a good track record.

An example of how expensive projects can get when prequalification does not take place comes from the renovation of the new MTA headquarters currently underway at 2 Broadway. Removal of hazardous material was contracted for \$1.3 million but reached \$7.8 million in January 2003, even before the work was complete. Demolition was budgeted at \$720,000, but ended up costing \$4.8 million. The installation of drywall was budgeted at \$411,000; but ended up costing \$9.5 million.⁶

As the Organized Crime Task Force concluded, the process of selecting contractors by city agencies would produce the best results when these agencies can choose from a list of contractors with good track records. Prequalification simply means the creation of such a list.

This report evaluates the state of responsible contracting practices in public works construction in New York City. As part of this evaluation the report examines the relationship between a contractor’s compliance with labor laws and the quality of its work, the quality of information about contracting that is provided by the Vendex System

³ Goldstock, p. 252.

⁴ Inspector General of the State of Massachusetts, “The Commonwealth’s Contractor Certification System: A Status Report”, 2000, emphasis added. <http://www.state.ma.us/ig/publ/contcerx.htm>.

⁵ The Construction Industry Partnership, no date; The American Council of Engineering Companies, “Response to Disaster Prominent Among Engineering “Academy Awards” Finalists,” Feb. 10, 2003.

⁶ Charles V. Bagli, “Sweet Deal for M.T.A. Home Turns Sour, Beset by Cost Overruns and Indictments,” The New York Times, 5/19/02.

and the effectiveness of the enforcement of labor laws in the city. Based on this examination the report also makes recommendation for improving the process of contracting in New York City.

1. Bad Employers Are Costly to Tax Payers

When contractors use unskilled and inexperienced workers the result is low quality and high cost to the government. Prevailing wage laws are designed to force contractors to use only qualified workers. The Inspector General of the U.S. Department of Housing and Urban Development (HUD) discovered a “direct correlation between labor law violations and poor quality construction” in 17 sites that his office investigated. This led him to conclude:

“Poor workmanship quality, in our opinion, results from the use of inexperienced or unskilled workers and shortcut construction methods. Roofing shortcuts result in leaks and costly roof and ceiling repairs. While shortcuts in painting may not be as serious, it does require future maintenance expense by requiring repainting sooner than anticipated. Electrical shortcut deficiencies are not as readily detected but may lead to serious problems such as fire and shocks . . . **Poor quality work led to excessive maintenance costs and increased risk of defaults and foreclosures . . . this systematic cheating costs the public treasury hundreds of millions of dollars, reducing workers’ earnings, and driving the honest contractor out of business or underground.**”⁷

Researchers at the University of Utah also discovered that bad contractors hurt both workers and taxpayers. They examined the effect of the repeal of prevailing wage law in Utah and eight other states.⁸ They discovered that following repeals:

Effect on Workers

- Injuries increased by 15%.
- Wages in the construction industry fell by 22%.
- Construction training declined by 40%. (The replacement of skilled with unskilled workers is perhaps the most important reason for the increase in injuries.)

⁷ “Audit Report on Monitoring and Enforcing Labor Standards,” Department of Housing and Urban Development, Office of Inspector General. Cited in Dale Belman and Paula Voos, “Prevailing Wage Laws in Construction: The Costs of Repeal to Wisconsin,” The Institute for Wisconsin’s Future, University of Wisconsin, January 1996 (revised), p. 5.

⁸ Peer Philips, Garth Magnum, Norm Waitzman and Anne Yeagle, “Losing Ground: Lessons from the Repeal of Nine “Little Davis-Bacon” Acts,” University of Utah, February 1995.

- After the repeal minority representation in training programs declined by 36%.⁹
- Pension and health insurance contributions/coverage declined.¹⁰

Effect on Budget

- Cost overruns on construction projects increased from 2.0% to 7.3% of accepted bids.
- Final project costs as a percentage of the state engineer's original estimate increased by 2%.¹¹ Two percent of the \$3.5 billion worth of construction projects that New York City currently has amounts to \$70 million.
- Lost income and sales tax receipts exceeded cost savings to the state government by at least 27%.¹²

As a result of such concerns, several Massachusetts cities, including Boston, went further than the state law and passed ordinances that decree that a responsible contractor is also an employer who pays prevailing wages, provides apprenticeships, and pays for workers' benefits. Boston passed its "Responsible Employer Ordinance" in 1998, and two years later Mayor Menino reported that the ordinance "required no major additional resources and appears to have had a successfully **preventive impact**." (Emphasis added.) The mayors of Cambridge, Springfield and Worcester issued similar assessments. (Statement Attached.)

Bad Employers Are Costly to New York City Tax Payers

The clearest indication that contractors who mistreat workers also short change tax payers comes from New York City itself. The Fiscal Policy Institute drew a random sample of 30 contractors who have performed construction work for the city and for whom there is an evaluation of the quality of work they have done. Among the 19 contractors *with no* labor law violations 1 contractor's work was rated as unsatisfactory and 1 was rated as marginal. The work of 13 was rated satisfactory, and the work of 4 was rated excellent. In contrast, among the 11 contractors *with* labor law violations, the work of 2 was rated unsatisfactory, the work of 4 was rated as marginal, and the work of 5 was rated as satisfactory. No contractor who had labor law violations received an excellent rating. See Table 1 below.

⁹ Ibid. figure 3.9

¹⁰ Peer Philips, "Kansas And Prevailing Wage Legislation," Prepared for the Kansas Senate, Labor and Industry Committee, Feb. 20, 1998, p. 49.

¹¹ P. 15,

¹² Philips et al., page 29

Table 1: Quality of Work of New York City Contractors by Labor Law Violations		
Labor Law Violations* Quality of Work**	No Labor Law Violations Percent	Labor Law Violations Percent
Unsatisfactory	5.3%	18.0%
Marginal	5.3%	36.0%
Satisfactory	21.1%	46.0%
Excellent	68.4%	0.0%
Total	100.0%	100.0%

Source: New York City Mayor of Contracts, Data for the years 1993-2002.

* Any labor law violations by the contractor in 1993-2002.

**Lowest performance evaluation for the contractor in 1993-2002.

Thus, a contractor with labor law violations is more than five times as likely to have a low performance rating (either unsatisfactory or marginal) than a contractor with no labor law violations.

The performance rating, which is done by the city agencies who hire the contractors, is determined by six factors: Work quality, cost, keeping to schedule, contract changes, record keeping and cooperativeness. Thus a low performance rating indicates that a contractor was costly to the city. It either delivered work of low quality, did not finish work on schedule, imposed additional costs on the city, or forced the city to allocate additional resources to monitor its performance.

It should be noted that instead of drawing a sample, in theory it is possible to construct Table 1 for the whole population of construction contractors. Unfortunately, the data provided by the Mayor Office of Contracts (MOC) makes such analysis prohibitively costly. First, the data about performance evaluations and the data about labor law violations reside in two different files, and the two files are not compatible with each other. Whereas the performance evaluations file contains contract numbers, the caution file does not. Second, there are often differences in the spelling of contractor names between the two files, a fact that means that merging the files would have to be done by hand rather than with the aid of a computer program. Yet there are more than 4,500 contracts with evaluations and more than 20,000 line entries in the labor law violations file (with many duplications). We discuss the issue of how the city manages the information about its contractors below, where we make suggestions of how to improve the Vendex system.

2. Demographic Profile of Construction Workers

When contractors violate labor laws they hurt, tax payers, workers, and workers' families. Many of the workers belong to minority groups and the level of their educational attainment is only moderate.

As their ages indicate (Table 2), construction workers support families. Seventy-five percent of construction trade workers are over 30.

Table 3: Age Breakdown of New York City's Construction Industry Workforce	
Age Cohort	Percent
18-30 Years	25.2
31-40 Years	35.2
41-50 Years	25.6
51+	14.1
Total	100.0
Note: Non-trade related occupations, e.g., support and administrative positions, were excluded from analysis.	
Source: Current Population Survey data pooled for three years: 2000/2002.	

As Table 3 shows, the construction industry is well integrated racially. Fifty-five percent of workers are non-white.

Table 3: Racial/Ethnic Breakdown of New York City's Construction Industry Workforce	
Racial Cohort	Percent
White Non-Hispanic	44.4
Black Non-Hispanic	21.6
Hispanic (of any race)	25.5
Other	8.5
Total	100.0
Note: Non-trade related occupations, e.g., support and administrative positions, were excluded from analysis.	
Source: Current Population Survey data pooled for three years: 2000/2002.	

While the level of traditional school-based education of construction workers is not high – fewer than 10 percent of construction workers have a college degree – those who complete apprenticeship programs in the skilled trades generally receive 3-5 years of on-the-job training and extensive classroom instruction.

Table 4: Educational Attainment in New York City's Construction Industry

<u>Education Level</u>	<u>Percent</u>
Less Than High School	28.3
High School	40.6
Some College (inc. vocational training)	22.6
College & Higher	8.4
Total	100.0

Note: Non-trade related occupations, e.g., support and administrative positions, were excluded from analysis.

Source: Current Population Survey data pooled for three years: 2000/2002.

There are currently 145,291 workers in the construction industry who live in New York City, according to the Current Population Survey.¹³ The number is lower if one uses establishment employment data, which show that there are 115,600 employees who work for New York City based firms.¹⁴ (Some differences between these two data series are to be expected. The Current Population Survey covers New York City residents; the establishment employment data covers construction employment in New York City. Another important difference is that the CPS includes self-employed; the establishment series does not.)

About 25 percent of all workers in the construction industry are in various non-trades occupations such as project managers, and other administrative and office personnel. The focus here is on workers in the construction trades. Table 5 below shows the occupational breakdown of workers in the construction trades. Carpenters, electricians, painters, brick and stone masons and plumbers are the most numerous among them.

¹³ Bureau of the Census, Current Population Survey, ORG data, 2002.

¹⁴ NYS Dept. of Labor, annual average, 2002.

**Table 5: Occupational Breakdown of New York City's
Construction Industry**

<u>Occupational Group</u>	<u>Percent</u>
Carpenters	28.8
Electricians	20.0
Painters, construction and maintenance	14.4
Brickmasons and stonemasons	9.4
Plumbers, pipefitters, and steamfitters	9.3
Roofers	3.4
Construction trades, n.e.c.	2.8
Insulation workers	2.4
Tile setters, hard and soft	1.7
Glaziers	1.5
Structural metal workers	1.5
Drywall installers	1.4
Plasterers	1.1
Concrete and terrazzo finishers	1.0
Paperhangers	0.7
Carpet installers	0.5
Total	100.0

Note: Non-trade related occupations, e.g., support and administrative positions, were excluded from this analysis.

Source: Current Population Survey data pooled for three years: 2000/2002.

3. Estimating the Number of Construction Workers Employed Under NYC Public Works Construction Contracts

The number of employees that contractors with public work contracts employ is not reported anywhere, and it must therefore be estimated. FPI used an input/output model, IMPLAN,¹⁵ to translate the dollar amount of contracts to number of workers employed. The city currently has \$3.5 billion worth of construction contracts of different durations underway. (Contracts issued by the School Construction Authority were excluded.) This

¹⁵ The IMPLAN model, originally developed for the Federal government, utilizes detailed data on national and local inter-industry economic transactions to model the interaction between the different sectors of the economy. The IMPLAN model shows an output of \$100,412 per employee in the construction industry in New York City. Using the Gross State Product series for the statewide construction industry prepared by the U.S. Bureau of Economic Analysis, BEA, yields an output per worker of \$79,309. Given that in New York City, construction of office buildings is more prevalent than in the rest of the state, the BEA figures validate the IMPLAN figures.

translates into roughly 11,700 workers.¹⁶ Thus, the size of the contractors-with-city-contracts-work-force is 8% of the size of the construction workforce that lives in the city. (Alternatively, the city-supported construction workforce translates into about 10% of all construction establishment employment in NYC.

4. High Productivity of Construction Workers and Large Economic Impact of NYC Public Works Contracts

Construction workers are productive, and this is why the prevailing wages in this industry are relatively high. According to the IMPLAN model, output per worker in this industry in NYC is more than \$100,400 per worker.

Expenditures in the construction industry have significant spill-over effects. According to the IMPLAN model each \$1 billion spent creates 9,959 jobs in New York City in the industry itself, 2,326 jobs in New York City in industries that supply the construction industry, and an additional 2,285 jobs in New York City in industries that cater to the increased demand for goods and services that is generated by the increase in income.

5. Limitations of the Vendex System

The Vendex system is a DOS-based system that is not available online and contains very little information.

Labor Law Violations: While the Vendex system does indicate whether a contractor has had violations, it does not contain any information regarding these violations. In the case of prevailing wage violations there is no indication of what the underpayment was, or how many workers were involved. Similarly, in the case of OSHA violations there is no indication of what the fines were, or why the citation was issued.

An examination of the Vendex report on one contractor, Volmar Construction, Inc. (attached), demonstrates how severe the problems with Vendex are. Volmar has been a repeat and serious violator of safety regulations, as its OSHA citations clearly show. Volmar had 4 serious violations in 1991, 10 serious violations and 4 repeat violations in 1992, 8 serious violations and 3 repeat violations in 1993, 1 serious violation in 1998, and 2 serious violations in 2002. The Vendex record of Volmar shows the existence of OSHA violations in only two years, and does not contain any information regarding the fact that these were multiple, serious and repeated violations. All Vendex says about the 8 serious violations and 3 repeat violations of 1993 is: "OSHA CITATION FINE UNDER INFORMAL SETTLEMENT." There is a similar cryptic statement regarding violations in 1995. There is no indication in Vendex that there were violations in 1991, 1992, 1998 or 2002.

¹⁶ After adjusting each contract's total cost to cost per year.

The lack of information about prevailing wage violations is equally problematic. In May of 1995, two employees brought prevailing wage complaints against a sub-contractor of Volmar, Horn Maintenance Corp., for work as laborers at Prospect Heights H.S. The complaints covered the period from May 1994 through January 1995. Horn subsequently received a willful violation in December 1995. This willful violation is not recorded in Vendex. In 1998, as a general contractor on an SCA job at Prospect Heights H.S., a non-willful violation was found of \$18,987.47 for five employees listed as asbestos handlers who worked for Volmar's sub-contractor Continental Env. Corp. The only information contained in Vendex is: "NON WILLFUL VIOLATION SETTLEMENT."

While a researcher may ask the Mayor's Office of Contracts for information regarding violations that do appear in Vendex, the response time is from 5 to 10 days, and the data is not provided electronically. Information about each contractor costs \$25.

Performance Evaluation: Vendex suffers from the same shortcomings regarding the information it contains about the quality of work done. A cost overrun gets a simple entry of "yes" without any indication of the sum involved and what percentage the overrun is of the initial estimate. A delay is treated in the same way, without indication of how long it was. The same applies to quality of work. To be useful, Vendex must include all this information and a narrative evaluation of the contractor's performance.

The lack of enforcement and performance information is an even greater problem. A report by the Mayor Office of Contracts, "Agency Procurement Indicators," for Fiscal 2002, attached, shows that the Department of Corrections performed only 15% of the evaluations that it was required to perform. The numbers for the Departments of Buildings and Sanitation were 36% and 51% respectively.

One additional problem diminishes greatly the value of the Vendex system: The same contractors appears in the system with many different names. This problem can be easily solved by including a taxpayer id number.

To be useful, the Vendex system should include:

A taxpayers ID Number

The same contractor appears in the system under different names. Including the ID number will permit the consolidation of information about each contractors

Prevailing Wage Violations: What was the prevailing wage, what was the wage paid, how many employees were underpaid, whether the violation was willful or not, and the basis for this determination. Fines and interest should also be recorded.

OSHA Violations: Severity of violations, whether repeated, whether willful, amount of settlement, accidents.

Tax Liens: All debt for workers' comp payments or tax delinquencies should be entered on the system.

Job Performance: The record should provide an evaluation of performance on past contracts. The evaluation should include dollar amounts of cost overruns, length of time for delays, and a narrative rating of the quality of the work.

6. Prevailing Wage Enforcement

Under State Labor Law, the City Comptroller is charged with enforcing prevailing wage compliance for all New York City contracts. However, the Comptroller's office only conducts investigations on a complaint basis. Analysis of data provided by the City Comptroller office shows that, for complaint cases, the losses to employees and the gains to contractors from prevailing wage violations are substantial. The Comptroller does not make available data on the precise nature of prevailing wage violations: What the prevailing wage was, how much workers were paid, and how many workers were involved.¹⁷ Nevertheless, the Comptroller provides some aggregated data, and these data reveal that several employees were underpaid by city contractors as much as \$17,500. Restitutions by contractors amounted in one case to more than \$400,000. In fiscal year 2002 the City Comptroller assessed underpayments of \$3,064,997 and in 2001 the assessment was of \$3,556,935. The office resolved 150 cases in 2002. It must be borne in mind that the Comptroller investigates only when there are complaints. The Comptroller does not initiate random investigations.

7. Need for Public Scrutiny

Because the Comptroller does not conduct random checks, and because workers may be fearful to complain or may not know their rights, public scrutiny is necessary to assure compliance with the prevailing wage law. Such scrutiny cannot occur without easy-to-assemble information.

Although the frequency of prevailing wage violations cannot be determined with accuracy, it appears that it may be pervasive. Our procedure for estimating the frequency of violations in the case of one occupation, carpenters (the largest occupation in the construction trades) is as follows. The prevailing wage for carpenters in 2002 ranged from \$33.48/hour (for heavy construction) to \$35.09 (commercial buildings). In 2002 there were 27,088 carpenters living in the city and of these, 1,508 earned more than \$33/hour.¹⁸

¹⁷ Unfortunately, the data provided by the Wage and Hours Division of the U.S. Dept. of Labor regarding violations of the Federal prevailing wage law (Davis-Bacon) are not any better.

¹⁸ Source: CPS.

It is not known how many of the carpenters who earned the higher sums worked for contractors-with-city-contracts. But we estimate that contractors-with-city-contracts employed 2,176 carpenters¹⁹. If we assumed all of the workers reporting the prevailing wage rate or higher worked on city public works contracts, AND that not a single union carpenter working on a commercial office building project in NYC was paid the hourly union scale, the number of workers earning the prevailing wage would still fall short of the estimated number of carpenters employed under city contract.

There is of course no substitute for random checks to ascertain how frequently the prevailing wage law is violated and to enforce the law. Our rough estimate shows how important these checks are.

Public scrutiny of the enforcement of labor laws is also necessary because too often contractors who have a record of repeat violations continue to get city contracts. According to a City Council staff report, the contractor Rapid Demolition was awarded a \$4.3 million Department of sanitation contract in 1999 even though at the time Rapid already had a history of unsafe demolition practices, and its Site Superintendent, Philip Schawab, had been convicted for bribing a U.S. Environmental Protection Agency compliance office, and had been convicted and incarcerated for failure to collect and pay payroll taxes.²⁰

Volmar Construction was awarded a new \$4 million DEP contract in December 2000 in spite of its long history of violations (listed above) and the fact that in September of 2000 it was suspended from bidding on or receiving any further work by the School Construction Authority.

Conclusion: The Need for Transparency and Prequalification in Contracting

A government is only as good as the vigilance of those it serves. In order for tax payers to be able to monitor their government they must have readily available and pertinent information and the time to process it. A revamped Vendex system that provides easy access will improve the transparency of the contracting process. An open prequalification process will give interested members of the public the opportunity to flag unworthy contractors before they are awarded contracts. The result would be savings to taxpayers and decent working conditions for workers.

¹⁹ The share of carpenters among all construction workers in the city is 18.6%.

²⁰ New York City Council Investigation Division, Broken: A Case Study of New York City Contracting Gone Bad. New York City Contracts – Rapid Demolition. April 2003.