

Davis Bacon Prevailing Wage Retirement Plans



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Definition

- The Davis-Bacon Act (DBA) (P.L. 97-470) requires that wages paid on federal public works projects equal the wages paid in the project's locale on similar, private construction jobs.
- This is known as the *prevailing wage* requirement.

The History

- The Labor Explanation
 - The purpose of the Act was to support labor unions by protecting them from underbidding by out-of-town contractors (see Attachment 1 at end of handout).
 - From DOL's own manual:
 - To protect communities and workers from the economic disruption caused by competition arising from non-local contractors coming into an area and obtaining federal construction contracts by underbidding local wage levels.

The History (Continued)

- The Alternative Explanation
 - The Davis-Bacon Act, which requires federal construction contractors pay their workers "prevailing wages," was passed by Congress in 1931 with the intent of favoring white workers who belonged to white-only unions over non-unionized black workers (see Attachment 2 at end of handout).

The History (Continued)

- Important Dates for Service Providers
 - 1932: enacted
 - 1935: “predetermination” language added/wage-setting methodology established
 - 1964: fringe benefit component added: **THIS IS WHY WE’RE INVOLVED!**

Requirements of the DBA

- Requires payment of locally prevailing wages and fringe benefits to laborers and mechanics employed on federal government contracts in excess of \$2,000 for construction, alteration, or repair (including painting and decorating) of public buildings or public works

Requirements of the DBA (Continued)

- Examples:
 - General Services Administration contracts to build federal office buildings
 - Department of Defense contracts to build military housing

Requirements of the DBA (Continued)

- Prevailing wages are determined in advance by the Department of Labor (DOL) National Office and included in the bid specifications for covered contracts

Requirements of the DBA (Continued)

- The language of the Davis-Bacon Act requires contractors and subcontractors to pay “all laborers and mechanics employed directly upon the site of the work, unconditionally not less often than once a week, and without subsequent deduction or rebate on any account, the full amount accrued at the time of payment, computed at wage rates not less than those in the advertised specifications, regardless of any contractual obligation which may be alleged to exist between the contractor or subcontractor and such laborers and mechanics.”

What Makes Up the “Prevailing Wage?”

- The Davis-Bacon “prevailing wage” is made up of two interchangeable components:
 - A basic hourly wage
 - Fringe benefits

What Makes Up the “Prevailing Wage?” (Continued)

- Along with the basic hourly rate listed on the wage determination, a fringe benefit will be listed for any classification for which fringe benefits were found prevailing. The total, including any fringe benefits listed, comprises the “prevailing wage” requirement.
- This obligation may be met by any combination of cash wages and creditable “bona fide” fringe benefits provided by the employer:

What Makes Up the “Prevailing Wage?” (Continued)

- The total, including any fringe benefits listed for the classification, may be paid entirely as cash wages;
- Payments made or costs incurred by the contractor for “bona fide” fringe benefits may be creditable towards fulfilling the requirement; or
- A combination of cash wages paid and “bona fide” fringe benefits may be used together to meet the total required prevailing wage.

What Makes Up the “Prevailing Wage?” (Continued)

- EXAMPLE:
 - A Davis-Bacon wage determination requires:
 - Basic hourly rate: \$10.00
 - Fringe benefit: \$ 1.00
 - Total prevailing rate: \$11.00

What Makes Up the “Prevailing Wage?” (Continued)

- EXAMPLE:
 - The contractor can comply by paying:
 - \$11.00 in cash wages; or
 - \$10.00 plus \$1.00 in pension contributions or other “bona fide” fringe benefits; or
 - \$9.00 plus \$2.00 in pension contributions or any combination of “bona fide” fringe benefits.

What Makes Up the “Prevailing Wage?” (Continued)

- EXAMPLE:
 - It **is** acceptable to pay the worker **less** than the actual basic hourly rate, so long as the total paid meets the prevailing wage requirement
 - This rule is often erroneously stated as requiring that **at least** the basic hourly rate must be paid
 - That is incorrect!

What Makes Up the “Prevailing Wage?” (Continued)

- EXAMPLE:
 - Note: under DBA, monetary wages paid in excess of the basic hourly rate may be used as an offset or credit to satisfy fringe benefit obligations, and vice versa
 - If fringe benefit contributions are credited towards fulfilling the basic hourly rate requirement in the wage determination, at least the basic hourly rate listed in the contract wage determination must be used in computing overtime pay obligations)
 - In this example where the actual hourly rate paid is less than the basic hourly rate, when overtime is paid, it must be calculated at one and one half times the basic hourly rate:
 - 1.5 times \$10.00, or \$15/hour

How Is the Prevailing Wage Established?

- The overall prevailing wage is based on specific categories of workers
 - It is established by the DOL's Wage and Hour Division
- The Wage and Hour Division releases wage determinations (via publication in the Federal Register) about ten days before opening bids on a contract
 - A contractor also may apply for a project wage determination, by filing Form 308 with the Wage and Hour Division. Project-specific determinations apply only to that project and expire 180 calendar days after they are issued, unless the contractor applies for an extension

To Whom Does the Prevailing Wage Apply?

- Applies to all mechanics and laborers employed on a job site, regardless of whether they are employed by the general contractor or a subcontractor
- Owners of the contracting company and their family members who perform work as mechanics or laborers on the site are also subject to the prevailing wage requirement

To Whom Does the Prevailing Wage **Not** Apply?

- Workers whose duties are primarily administrative, executive, or clerical are not covered.
- Foremen who devote more than 20% of their time during a work week to mechanical or laborer duties **are** laborers and mechanics for such time

State Prevailing Wage Laws

- At least 35 states have their own “little” Davis-Bacon laws, usually called Prevailing Wage laws
 - States provide their own wage determinations for their state and municipal funded contracts
 - Operation is basically similar to the federal law

Allowable Fringe Benefits for Davis-Bacon Purposes

- Life insurance
- Health insurance
- Pension
- Vacation
- Holidays
- Sick leave

Benefits Not Allowed for Davis-Bacon Purposes

- No credit may be taken for any benefit required by federal, state, or local law, such as:
 - Workers compensation
 - Unemployment compensation
 - Social security contributions
 - Health benefits required under Hawaii state law
- The use of a truck is not a fringe benefit
- A Thanksgiving turkey or Christmas bonus is not a fringe benefit

Meeting Davis-Bacon Requirements with Qualified Plan Contributions

- Contributions to a qualified plan may be counted toward meeting the prevailing wage requirement
 - Money purchase plans were the norm previously
 - Provided maximum bang for the buck
 - Profit sharing or 401(k))plans may also be used and tend to be the common approach now
 - Due to the fact that deductible PS limits are now the same as MP plans
 - Defined benefit plan may be used, but such use is rare

Meeting Davis-Bacon Requirements with Qualified Plan Contributions (Continued)

- Master and Prototype Plans
 - Rev. Proc. 2000-20, section 5.03, permits non-standardized master/prototype plans to provide non-uniform allocation formulas that are designed to accommodate the Davis-Bacon prevailing wage requirement

Meeting Davis-Bacon Requirements with Qualified Plan Contributions (Continued)

- It is common that an employee has both Davis-Bacon wages and non-Davis-Bacon wages within the same year
 - A separate plan can be established just for the Davis-Bacon contributions, but that is not required
- Alternatively, a plan may provide within it a special allocation or contribution formula that credits an employee with dollars based on his or her Davis-Bacon hours only

Meeting Davis-Bacon Requirements with Qualified Plan Contributions (Continued)

- The contractor must make payments or incur costs in the amount specified by the applicable wage decision **with respect to each individual laborer or mechanic**
 - Thus, the amount contributed for each employee must be determined separately, and credit is taken accordingly towards the prevailing wage requirement for each individual

Meeting Davis-Bacon Requirements with Qualified Plan Contributions (Continued)

- Contributions to fringe benefit plans must be made regularly, not less often than quarterly
 - Annual contributions into a plan do not meet this requirement
 - While profit sharing plans are bona fide within the meaning of the Act, profits are not usually determined until the end of the year
 - Therefore, the DOL requires contractors to escrow money at least quarterly on the basis of what the profit sharing contribution is expected to be

Meeting Davis-Bacon Requirements with Qualified Plan Contributions (Continued)

- The plan may not require a minimum number of hours for the plan year, nor employment on the last day of the plan year, as a condition for receiving the contribution allocation

Meeting Davis-Bacon Requirements with Qualified Plan Contributions (Continued)

- Vesting provisions are permissible
 - An employee who leaves employment before completing the specified length of service may forfeit all or part of the accrued benefit
 - Such forfeitures are permitted, provided the plan is a bona fide plan that meets applicable requirements under ERISA, including minimum vesting requirements
 - Forfeited Davis-Bacon contributions may not revert to the employer, but should be distributed among the remaining plan participants

Meeting Davis-Bacon Requirements with Qualified Plan Contributions (Continued)

- Vesting provisions are permissible
 - However, if you use a Davis-Bacon defined contribution plan and **do not** provide full vesting, you will be subject to the *annualization* requirements
 - See below
- Most Davis-Bacon plans provide full and immediate vesting

Why Use a Qualified Plan in a Davis-Bacon Situation?

- Paying the full fringe rate in cash through wages places the contractor at a competitive disadvantage on their labor costs vis-a-vis a contractor providing fringe benefits

Why Use a Qualified Plan in a Davis-Bacon Situation? (Continued)

- Higher payroll taxes are incurred on the additional cash used to meet the fringe benefit requirement
 - FICA
 - Workers Compensation
 - This can be a very large cost in many construction industries
 - FUTA (Federal Unemployment Tax)
 - SUTA (State Unemployment Tax)

Why Use a Qualified Plan in a Davis-Bacon Situation? (Continued)

- Example
 - Assumptions:
 - Base hourly rate of \$20.00
 - Fringe rate of \$5.00
 - The table on the next slide demonstrates the savings as a result of providing benefits versus paying the fringe rate in cash

Why Use a Qualified Plan in a Davis-Bacon Situation? (Continued)

	No Benefits - Paying All Cash	Providing Benefits
Cash Wages	\$25.00	\$20.00
Fringe paid to benefit plans	0.00	5.00
Payroll burden (assume 20%)	5.00	4.00
Total Cost Per Hour	\$30.00	\$29.00

*Annual Saving Per Employee (assume 2080 hours): **\$2080.00***

Special Nondiscrimination Rules and Testing Exceptions for Davis-Bacon Plans

- There aren't any!
- There are no regulations under the coverage rules of IRC §410(b) or the nondiscrimination rules of IRC §401(a)(4) that provide special treatment of Davis-Bacon plans

Special Nondiscrimination Rules and Testing Exceptions for Davis-Bacon Plans (Continued)

- Davis-Bacon employees (or at least the wages attributable to Davis-Bacon work) are by definition non-union employees (or nonunion wages), so the coverage exclusions and disaggregation rules pertaining to collectively bargained employees would not apply to plan contributions made with respect to Davis-Bacon wage fringe requirements

Special Nondiscrimination Rules and Testing Exceptions for Davis-Bacon Plans (Continued)

- In some cases, a plan that covers only Davis-Bacon wages or a plan that covers only non-Davis-Bacon wages might not satisfy coverage and/or nondiscrimination requirements, necessitating redesign of the plan or, if available permissive aggregation with another plan so that these requirements can be satisfied (See Treas. Reg. §1.410(b)-7(d))

Special Nondiscrimination Rules and Testing Exceptions for Davis-Bacon Plans (Continued)

- Be especially careful of highly compensated employees (such as the owner's children) who might receive DBA contributions and cause testing problems
 - Solution: exclude the HCE from the Davis-Bacon plan
 - You will have to provide this individual the additional fringe benefit rate in their pay, but that is usually not a problem for family members
 - It will also make passing the various tests much easier since you are excluding an HCE who will be receiving zero benefits!

Special Nondiscrimination Rules and Testing Exceptions for Davis-Bacon Plans (Continued)

- Likewise, if the plan is a 401(k) plan, you must still pass all the regular 401(k) and 401(m) testing
 - The Davis Bacon contributions to the 401(k) plan can be used in 401(k) and cross testing
 - This can be very useful if the plan is not otherwise a safe harbor plan

Special Nondiscrimination Rules and Testing Exceptions for Davis-Bacon Plans (Continued)

- You will need to pay attention to the definition of compensation under IRC §414(s)
 - Compensation under IRC §414(s) includes both Davis-Bacon and non-Davis-Bacon wages
 - There is no “safe harbor” definition that permits a non-Davis-Bacon plan to disregard Davis-Bacon wages or a Davis-Bacon plan to disregard non-Davis-Bacon wages to determine if the applicable coverage and nondiscrimination testing requirements are satisfied

Annualization Requirement

- Davis-Bacon credit for contributions made to fringe benefit plans are allowed based on the effective annual rate of contributions for all hours worked during the year by an employee

Annualization Requirement (Continued)

- Examples:
 - For a defined benefit pension plan, or for a defined contribution pension plan that does **not** provide for immediate (or essentially immediate) vesting, if a contractor wishes to receive \$2.00 per hour credit for a pension contribution, the contractor must contribute at this same rate for ***all hours worked during the year*** (both Davis-Bacon and non-Davis-Bacon hours)!
 - If this is not done, the credit for Davis-Bacon purposes would have to be revised accordingly

Annualization Requirement (Continued)

- Examples:
 - If the firm's contribution for the pension benefit was computed to be \$2,000 a year for a particular employee, the employee worked 1,500 hours of the year on a Davis-Bacon covered project and 500 hours of the year on other jobs not covered by the Davis-Bacon provisions, only \$1,500 or \$1.00 per hour would be creditable towards meeting the firm's obligation to pay the prevailing wage on the Davis-Bacon project
 - Annual contribution (\$2,000), divided by total hours worked (1,500 + 500 = 2,000); i.e. $\$2,000 / 2,000 \text{ hours} = \1.00 per hour

Annualization Requirement (Continued)

- This is not a particularly desirable result unless employees work almost exclusively on Davis-Bacon projects during the year

Annualization Requirement (Continued)

- For contributions made to defined contribution pension plans that provide for immediate participation and immediate (or essentially immediate) vesting schedules (100 percent vesting after an employee works 500 or fewer hours), a contractor may take Davis-Bacon credit at the hourly rate specified by the plan
- Under such plans, contributions are irrevocably made by the contractor, most, if not all, of the workers will become fully vested in the plan, and the higher contributions made during Davis-Bacon work result in an increase in the value of the individual employee's account
 - The amount of contributions to such plans must be in conformance with any limitations imposed by the Internal Revenue Code

Annualization Requirement (Continued)

- An employee works as an electrician where the wage determination rate is \$12.00 (basic hourly rate) plus \$2.50 in fringe benefits. The employer provides the electrician with a retirement contribution of \$1.20 per hour. If the employee in this example receives no other “bona fide” fringe benefits, then for each hour worked on a covered contract the individual is due \$12.00 (basic hourly rate) plus \$1.30 paid as cash (the difference between the \$2.50 per hour fringe benefit required under the applicable wage determination and the credit allowed for the provision of retirement benefit.) Thus:

Basic hourly rate	\$12.00
Retirement benefit	1.20
Additional cash due	<u>1.30</u>
Total due per hour	\$14.50 (\$12.00+\$2.50)

Maximizing the Davis Bacon Plan

- In this example (\$12.00 basic hourly rate + \$2.50 fringe benefit), how would we maximize the *employer's* benefit?
 - Assume no other fringe benefits
 - Assume 25 percent deduction limitation
 - $\$14.50 \times .8$ = \$11.60 hourly rate
 - 25 percent plan contribution = \$ 2.90 per hour
 - Total hourly cost: = \$ 14.50

Maximizing the Davis Bacon Plan (Continued)

- It is possible to increase the contribution beyond 25 percent of the hourly rate paid since the 25 percent limit is an *employer* deduction limitation and not a Section 415 limit
 - Remember, the employee can have up to 100 percent of his or her compensation

Maximizing the Davis Bacon Plan (Continued)

- Thus:
 - If there were enough room for the employer deduction (that is, sufficient other non-Davis-Bacon wages paid), the employer could pay an hourly rate of \$7.25 with a corresponding contribution to the plan of \$7.25/hour (subject to the overall 415 dollar limit)
 - This should definitely be considered where the Davis-Bacon work is a small percentage of the overall employer's revenue and there is not another significant retirement plan benefit in effect (or other fringe benefits)

Offset Arrangement

- A qualified plan may offset Davis-Bacon amounts against any other allocations that might be provided under the plan
 - For example, the Davis-Bacon contribution might help satisfy the safe harbor contribution obligation under a safe harbor 401(k) plan, or the “gateway” contribution requirements under a cross-tested defined contribution plan
 - The following example, which appeared in Amy Cavanaugh’s article on Davis-Bacon plans in the May-June 2003 ASPPA Journal, demonstrates how an offset might work

Offset Arrangement (Continued)

- A money purchase plan requires a ten percent contribution for all eligible employees
 - The plan includes a Davis-Bacon feature that is designed to offset the required contribution
- The Davis-Bacon fringe piece for the year in question is \$6 per hour
- Pursuant to the Davis-Bacon feature in the plan, the employer contributes an amount for each employee that equals \$6 times the number of Davis-Bacon hours.

Offset Arrangement (Continued)

- In addition, under the non-Davis-Bacon feature in the plan, the employer contributes the lesser of:
 - Ten percent of the employee's total compensation (column (6) of the table on the next slide);
 - Or the amount above reduced by the contribution made pursuant to the Davis-Bacon feature (i.e., the offset amount), as shown in column (7) of the table on the next slide
 - If the Davis-Bacon contribution exceeds ten percent of total compensation, the employer makes no additional contribution for the employees

Offset Arrangement (Continued)

1 Employee	2 DB Wages	3 Non-DB Wages	4 Total Wages	5 DB Hours	6 10% of Wages	7 DB Contrib.	8 Non DB Contrib.
Bob	\$0	\$200,000	\$200,000	0	\$20,000	\$0	\$20,000
Bill	\$25,000	\$25,000	\$50,000	1000	\$5,000	\$6,000	\$0
Ben	\$10,000	\$20,000	\$30,000	400	\$3,000	\$2,400	\$400

Sources for Assistance

- The Department of Labor publishes the Prevailing Wage Resource Book, a 250-page plus document that provides an enormous amount of helpful information about how Davis-Bacon (and some other similar federal programs) operate. You can find this resource at:
 - <http://www.wdol.gov/docs/WRB2002.pdf>
 - This is the 2002 version and it is in a single PDF file
 - <https://www.dol.gov/whd/recovery/pwrb/toc.htm>
 - This is the 2015 version but it is in 22 individual chapter PDFs

Sources for Assistance (Continued)

- Amy Cavanaugh, CPC, QPA, QKA had an excellent article in the May-June 2003 issue of the ASPPA Journal. In addition, Amy authored the Davis-Bacon column on BenefitsLink that can be found at:
 - http://benefitslink.com/modperl/qa.cgi?db=qa_davisbacon
- The complete printout of Amy's BenefitsLink Q&As (as of November 11, 2004) can be found as Appendix I of additional PDF file.

Questions?

