New York State Department of Labor
David A. Paterson, *Governor*
Colleen C. Gardner, *Commissioner*

May 10, 2010

[redacted]

Re: Your letter of March 3, 2010
[redacted]
Our File No. RO-10-0033
PRC No. 04-8053

Dear [redacted]:

You have asked for Counsel's opinion regarding [redacted] compliance with the prevailing wage law in regard to [redacted] payment of supplemental benefits earned by workers on public work projects. On behalf of your client, you contend that payments made into [redacted] Employee Retirement Plan, on behalf of those employees, satisfies the prevailing wage law's requirement that supplements be paid to the employees in either cash or equivalent benefits. As you know, [redacted] is under investigation by the Bureau of Public Work in regard to this very issue in at least two prevailing wage cases, and you have an opinion from the Bureau of Public Work indicating that such contributions to a retirement plan are subject to annualization pursuant to 12 NYCRR §220.2. The opinion of the Bureau is correct in regard to the requirement that these contributions be annualized.

A review of the summary plan description related to [redacted] "employee retirement plan" indicates that the employer is depositing supplemental benefits required to be paid to employees by the prevailing wage law (referred to as the "Qualified Non-Elective Contribution - QNEC) into the plan in lieu of paying cash to the employees (it is noted that the plan apparently indicates that contributions of supplements offsets any discretionary payments made by the employer to the plan, thereby rendering workers who receive supplements ineligible to receive employer contributions. It is further noted that the plan defines QNEC in two contradictory manners, first as a percentage contribution requiring 800 hours of work to vest, and later as a contribution of required supplemental payments "to help satisfy the fringe benefit requirements of the law"). Employees for whom required supplements are paid into the plan are immediately vested in the plan, and all contributions made by the employee, including supplements that are paid to the plan, plus any additional contributions made by the employee to the plan are all available to the employee upon termination of employment. In the event that employment is

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terminated such funds must be rolled over into another plan or they become fully taxable after 60 days. In general, such payments to benefit plans are acceptable by the Bureau, subject to the annualization regulation set forth in 12 NYCRR §220.2. The regulation provides that whenever supplements are not paid in cash in accordance with 12 NYCRR §220.2(b) (providing for cash payment of supplements), the "cash equivalent" of supplements provided on behalf of workers is obtained by dividing the actual amount contributed by the total hours worked on both public and private projects 12 NYCRR §220.2 (d)(1).

[redacted] contests this method of computing the cash equivalent of contributions on the ground that the Court of Appeals in *Chesterfield v NYS Dept. of Labor,* 4 N.Y. 3d 597 (2005) limited its holding to projects in which the contractor contributed into a profit sharing plan for both public and private work. The applicable language, quoted in your letter, reads as follows:

> "Because Chesterfield contributed to the profit-sharing plan not only for its employees' public work but also for their private work, however, there was room for shifting costs on paper to overstate its payments on behalf of public hours, which would have bestowed an unfair competitive advantage on Chesterfield and denied its employees the full value of the supplements to which they were entitled. To enforce against this potential cost shifting, the Commissioner chose to average Chesterfield's contributions over all work, both public and private, to which pension benefits might be related. This resulted in a proportionate credit to offset Chesterfield's supplement obligations. We cannot say that the Commissioner acted unreasonably or irrationally in taking this approach under the circumstances of this case."

The Department's annualization of contributions made to health and pension plans has been subject to a long history of litigation, which will be summarized here for purposes of placing [redacted] argument into its proper context. There are six recent major cases that discuss the Department of Labor's policy with regard to the manner in which it treats amounts contributed to employee benefit plans on public work projects. The first case is *General Electric v New York State Department of Labor*, 891 F2d 25. In that case, a divided court determined that to the extent that Labor Law Section 220 required either the type or amount of an employer's contribution to an ERISA plan, that law "relates to" employee benefits in that it "has a connection with or reference to such a plan" and is therefore preempted by ERISA. In large part, this determination was based upon the then existing policy that specific benefits be provided in specific amounts by the Commissioner, and that an employer was not permitted to substitute one form of benefit or supplement for another.

In the second case, *Burgio v NYS Dept of Labor*, 107 F3d 1000 (2nd Cir. 1997), the court held that a "total package" approach, whereby the prevailing wage law required a total sum for all benefits but did not require any specific contributions to any form of plan, was not preempted by ERISA because such a requirement affected employee benefit plans "in too tenuous, remote, or peripheral a manner to warrant a finding that the law "relates to" the plan *Burgio v NYS Dept of Labor*, 107 F3d 1000 (2nd Cir. 1997). As opposed to the GE plan, the contractor, not the

Commissioner, determines the type of supplements to be provided. In those circumstances, *Burgio* held that no preemption applied.

The third case is *HMI Mechanical Systems v McGowan*, et. al, 266 F3d 142 (2nd Cir., 2001). In that case, the plaintiff challenged the Department's annualization formula used to calculate the hourly cash equivalent of supplements paid to workers on public work projects, claiming that ERISA had preempted state regulation of the subject. The court held that:

> "The annualization formula calculates the level of prevailing supplement contributions by dividing the employer's total actual contribution on behalf of its workers by the total annual hours (both public and private) that an employee worked. According to HMI, this formula always results in a shortfall in its contributions if an employee performed any private work during the period analyzed. However, that is precisely the desired effect of Section 220, which creates an economic disincentive for employers to use pooled supplement plans. The information that the state requires to apply the annualization formula is precisely what we contemplated in *Burgio*. Id. Furthermore, the formula on its face is concerned with the level of the employer's contribution rather than the benefit that any worker receives, so it is consistent with the total package approach. Simply because the annualization formula devalues employers' total contributions does not make it an improper line-item examination of ERISA benefits." *HMI Mechanical Systems v McGowan*, et. al, 266 F3d 142 (2nd Cir., 2001).

As a result, the court held that the Department's use of the annualization formula did not violate ERISA preemption.

The fourth case is *Rondout Electric v NYS Dept. of Labor*, 335 3d 162 (2nd Cir., 2003). There, on facts identical to those put forth by [redacted] in regard to its retirement plan, the court considered whether the State's annualization regulation, 12 NYCRR §220.2(a), was preempted by the National Labor Relations Act (NLRA). The court specifically noted that the retirement plan provided that workers' supplements, earned on public work projects, were contributed to a retirement plan, but that no supplement payments were made on private projects. Each employee had a separate retirement account, which was self-directed. The Department, using the annualization regulation, audited the projects in question and credited Rondout with the payment of supplements by dividing the total hours worked in a year by the total payments made into the plan. The court, noting its approval of the annualization regulation in the *HMI* case, determined that the annualization regulation was not designed to encourage or discourage employees in the promotion of their interests collectively. Without some connection between the payment of prevailing wage supplements and labor/management bargaining, the court determined that the annualization regulation did not come within the sphere of *Machinists* preemption under the NLRA. The court noted that while certain tax implications might have an indirect impact on the bidding process, that nothing in the regulation imposed a specific choice on either employee or employer.

Therefore, the annualization regulation did not fall within the scope of the NLRA and was not preempted by it.

The fifth case is the Chesterfield matter in the New York Court of Appeals, cited above and discussed below. The last case, is *United States v Coren*, 2008 U.S. Dist. Lexis 71564, notable for its accurate summation of the law in this regard. After reviewing the relevant cases, the court held that:

> "Taken together, the plain meaning of the language of the statute, its legislative history, regulatory clarifications and related interpretive caselaw gave more than fair warning that conduct such as charged here is criminal--prevailing wage credit cannot be claimed where it is intended beforehand that the workers on whose behalf the credit is taken will be ineligible to share the benefit. As applied, Davis-Bacon and Section 220 do not appear vague given the charges are grounded upon Coren's alleged participation in devising and executing such a scheme to defraud federal and state agencies by intentionally claiming false prevailing wage credits for corresponding deposits made to the CBT. Whether the government can prove all that it alleges beyond a reasonable doubt, of course, is a matter for trial. What the indictment alleges, however, is enough to withstand Coren's constitutional challenge **[*38]** by motion before trial."

In *Coren*, the court found the law and cases to be sufficiently clear to form the basis of a criminal charge against a defendant who sought to overstate the value of supplements actually paid to the employees. The court's discussion of the law in this regard indicates that there is no remaining dispute as to the applicability of the annualization regulation in prevailing wage cases.

This point of law, as demonstrated above, has been litigated for the better part of two decades, and no court has held that the Department's annualization regulation cannot be enforced. Rather, every court that has considered the issue has determined that the regulation is a valid exercise of the State's authority to enforce the prevailing wage law.

According to [redacted] the fact that it contributes nothing to the plan for private work prevents it from "shifting costs" as noted by the Court of Appeals and distinguishes this plan from all others. First of all, the interpretation of the Court's language urged by [redacted] is simply wrong. The Court was not setting up a distinction between types of plans, but merely observing that benefits that were being paid to employees in public work projects were contributed to the profit sharing plan. The court was not distinguishing between a plan supported by public project contributions as opposed to public and private contributions, but rather noting that any plan to which public work contributions were made created an unfair competitive advantage to Chesterfield and denied its employees the full value of their contribution. The court was not pointing the way to an alleged exception to the well established rule regarding the propriety of the annualization regulation. The interpretation of the Court's language urged by [redacted] has no basis in the existing case law.

In fact, the failure to contribute anything on private work enhances the benefit derived by [redacted] in "shifting costs." [redacted] actually contributes nothing to the plan in this matter.

Rather, it uses money that is required to be paid to employees on public work projects to create retirement accounts on their behalf. [redacted] advantage is enhanced by the fact that it pays nothing toward retirement in its private work, but funds the entire cost of the retirement plan through its public work, a phantom benefit to the public work workers, since it is their money that provides the benefit. Some contractors, however, pay supplements on all of the work they perform, be it public or private. When [redacted] gets to lower its overall costs by only paying supplements on a portion of their work, they obtain a competitive advantage that tilts the playing field in their favor when bidding on public work contracts. The intent of the public work statute and the Commissioner's regulation is to insure that all bidders have equal labor costs, thereby rendering labor costs irrelevant to the bidding process. That intent has been approved by the courts for almost twenty years, as noted above.

The holding in *Chesterfield* did not revolve around this subject, but rather approved of the annualization formula as a means of leveling the bidding playing field. The court states that "annualization is a methodology for valuing fringe benefits, which the Commissioner reasonably applied here to compute the hourly cash equivalent of *Chesterfield's* contribution to its profit sharing plan."

In this matter, the retirement plan sponsored by [redacted] is nothing more than a savings plan whereby employees, who are entitled to supplemental benefits, are forced (employees are given no option in this regard) to have those benefits paid into a company sponsored retirement plan. By doing so, [redacted] obtains substantial savings in taxes that would otherwise be incurred in paying supplements in cash.[1] And while the employees obtain some benefit in that the money put aside vests immediately to their behalf, for the most part, such sums are not available to them until they leave the employ of [redacted] and, even then, are subject to IRS penalties if withdrawn early and federal taxes upon withdrawal. Under these circumstances, the workers do not obtain the benefit to which they would otherwise be entitled had they been paid in cash. In these circumstances, the Commissioner is required to compute the hourly cash equivalent of the contribution, and has done so in a manner previously approved by the Court of Appeals and the Federal Courts as noted above.

To summarize, the plan submitted by [redacted] is not significantly different from the plan that was before the Court of Appeals in *Chesterfield* and in *HMI*. In both cases, the Commissioner has properly valued the contribution to the plan, and the Court of Appeals confirmed that methodology. [redacted] "contributions" to the workers' retirement plans must be annualized. As noted by the Bureau in its memorandum as to these issues, any challenge to the manner in which the Commissioner values supplemental payments into a plan should be raised in the context of an administrative hearing as to underpayments of wages and supplements as determined by the Bureau of Public Work. The Court's language in *Chesterfield* does not alter,

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[1] For every dollar in payroll, an employer must pay an additional 7.65 % F.I.C.A., 7 % in workers' compensation insurance, and 2.7 % in general liability insurance. Thus, the actual cost to an employer is approximately $ 1.17 for every cash dollar that the employer pays its employees for prevailing wage supplements.

and in fact confirms, the existing policies of the Department of Labor in regard to its annualization of benefits in the circumstances described by [redacted]

Very truly yours,

John D. Charles
Associate Attorney

JDC:cmh

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