

The Proposed Regulations and Guidance Implementing the “Fair Pay and Safe Workplaces” Executive Order will Impose Substantially Higher Costs than the Administration Estimated

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Overview

The measurable initial year costs for implementation of the regulations and guidance associated with E.O. 13673, “Fair Pay and Safe Workplaces” will very likely be \$5 billion to \$11 billion with subsequent, on-going annual costs between \$3 billion to \$7.0 billion. In addition to measurable costs, there are many costs that are currently immeasurable due to uncertainties in how the E.O. will be applied, or practical consequences that while easily anticipated, are not currently quantifiable.

The Chamber’s comments submitted to the rule making docket in August 2015 illustrated that correction of just a few of the administration’s errors would result in a ten-fold revision of the administration’s cost estimate to approximately \$1 billion per year, but that was determined by a limited amount of preliminary data. A full cost accounting using more extensive and experiential data would result in a total much higher. The opportunity to collect data was limited by the too-short comment period set by the administration. Since the submission of our comments, the Chamber has continued to conduct interviews of experienced contract management professionals, and the data obtained confirms that the expected cost of the measureable impacts will be at least \$5 billion for the initial year and at least \$3 billion for each year thereafter.

In contrast, the administration’s aggregate estimate of \$107 million in initial year compliance costs and \$92 million in subsequent yearly costs is a grossly under-counted and unrealistically optimistic forecast. Accordingly, because of the high potential cost and the large range of uncertainty, especially on the upper end, this rulemaking clearly needs more careful analysis informed by facts and data. The potential costs are too high to risk conducting this field experiment on the American economy and the American taxpayer.

This paper summarizes the factors and data that contribute to this higher estimate of costs, and identifies several of the currently unquantifiable, but real, costs that will result in even higher cost burdens than what can be estimated currently.

Discussion

The administration’s cost estimates were developed without adequate data and ignore many important factors.

This rule was developed in a rush without adequately assessing the full cost burdens and complications that it would add to the procurement system and impose on affected employers. The administration also ignored input and concerns from those who will be affected by it, leaving the administration with only bad information and wishful thinking on which to base their compliance cost estimate. The errors and omissions in the analysis mean that the likely cost is at least an order of magnitude greater than the government’s estimates, and the range of uncertainty is so great that the risk of an extreme compliance cost over-run is highly likely.

Among the government errors driving its low estimate are:

- Underestimating the number of companies that would be affected;
- Omitting the significant costs of setting up and maintaining information systems to collect and verify information required by the rule;
- Grossly under-estimating the amount and cost of labor time that would be required to comply with the proposed reporting and tracking requirements, especially the costs of providing supplemental information to ensure proper evaluation of administrative merits determinations; and
- Most significantly, failing to realistically account for the administrative costs, bidding process delays and potential legal liabilities imposed by the proposed requirement to make prime contractors responsible for managing regulatory compliance of their subcontractors.

The administration did not take the time and effort to do the basic field research about business processes, experiences and costs that any reasoned regulatory decision requires. Furthermore, the administration refused requests from the affected business community to extend the comment period sufficiently to allow the Chamber and others to collect accurate and meaningful compliance cost data. Despite this refusal to provide an adequate comment period, the Chamber proceeded as best it could in the limited time provided in 2015 to identify and interview knowledgeable contract managers, labor law compliance attorneys, and others regarding the compliance cost elements of the proposed rule. The Chamber's comments provided an extensive analysis of the errors and omissions in the Administration's cost analysis, and provided a roadmap for gathering additional data and improving the completeness of the cost analysis. The Chamber has built upon that foundation as it has continued to compile new data since the end of the too-short public comment period August 28, 2015.

As noted previously, the measurable initial year costs will most likely be \$5 billion to \$11 billion and subsequent, on-going annual costs will be \$3 billion to \$7 billion per year. These cost estimates are based on data regarding the time and labor costs of compliance with the proposed regulation provided by contractors' managers, information systems specialists and attorneys who practice in the Federal contracts area in response to interviews conducted over the past year. Specific questions were asked regarding the incidence of reportable events, the time and cost to document information about reportable cases, the time and cost of evaluating potential subcontractors, the incidence and cost of defending award protests and the costs of constructing and maintaining information systems to track required information. A breakout of specific factors and their contribution to the higher cost estimates is included as Appendix 1.

Additional Costs are Foreseeable but Currently Unmeasurable.

There are also many additional costs that are harder to measure in advance, but that will show up as real if a rule is implemented. All of these costs – those that can be estimated in advance and the harder to measure ones – will ultimately be passed along to the American taxpayer in higher costs on Federal procurements. With Federal contract procurements currently at \$450 billion per year, the measurable costs *alone* would add a full percent or more to the expense of Federal procurements.

Among the costs that cannot currently be measured, but will unequivocally occur, are the following. These are further discussed in Appendix 1:

1. Increased incidence and legal costs of contract award protests by bidders who are turned down because of labor law compliance allegations or by bidders who claim that their better records were not weighed heavily enough in the award decision;
2. Delays in the procurement process because of the burden of submitting and evaluating supplemental information required by this regulation;
3. Litigation costs and delays related to the role that the regulation will impose on prime contractors to evaluate the labor compliance records of subcontractors; prime contractors will be exposed to “disparagement” lawsuits seeking damages by prospective subcontractors who are not chosen to join a bid because of the prime’s evaluation;
4. Costs and uncertainties that this regulation adds to the procurement process will discourage companies from bidding for Federal contracts, reducing competition and leading to higher costs for government support services;
5. Increased litigation cost and incidence resulting from the prohibition on arbitration agreements for contracts over \$1million; and
6. Tracking and reporting of “equivalent state laws.” While unknowable due to the absence of guidance as to what constitutes an equivalent state law, this factor will be substantial.

Furthermore, the uncertain impacts of key elements of the proposal mean that the compliance costs could significantly over-run the dollar amounts presented here. Given the many uncertainties, especially how this rule will affect the incidence of contract award protests and related legal challenges, significantly higher impacts are expected. There are so many unresolved questions and uncertainties surrounding the impact of this expansive and ambiguous regulation that there is a high likelihood that the cost impact will be much greater than the \$5 billion to \$11 billion initial and \$3 billion to \$7 billion in subsequent years based on our analysis. While \$3 billion defines the ongoing annual cost floor, the upper end of the potential cost distribution is unknown: it could exceed the top end of the range shown under some scenarios. There are simply too many unknowns to put a certainty cap on the cost impact. This means that finalizing the rule as proposed will subject the government procurement system and the U.S. economy to a very risky and potentially costly experiment. This uncertainty argues for withholding a final rule until further fact-gathering and analysis can better determine the true cost impact of this regulation.

Appendix 1: Breakout of Specific Cost Factors Not Included in the Administration's Estimate

The administration's estimate of initial year cost of \$106 million increases to \$5 billion when the following items are included:

1. Correction of individual compliance activity assumptions to reflect estimates based on interviews with experienced contract managers; adjustments average 4x original estimate.
2. Correction of labor time opportunity cost amounts to reflect estimated full overhead load based on Federal contract data; adjustment is 3.3 x base labor wage based on our comparative analysis between administration projections and input received from companies.
3. Adjustment of labor category; in many cases the administration analysis assumes that a clerical worker performs tasks that experienced contract managers said should be handled by managers or professionals at \$55 to \$65 per hour wage rather than \$25 per hour wage assumed in administration estimate.
4. Correction of administration estimate of 20,139 affected contractors. The administration's estimate failed to account for instances where the \$500,000 contract value threshold required by the rule was reached through a series of smaller orders under the same contract totaling \$500,000 or more. Many indefinite quantity or task order contracts have a cumulative value in excess of the threshold and will be covered by the rule even though no single order under the contract exceeds \$500,000. The administration's estimate of 20,139 affected contractors only reflected instances where a contractor received a single payment of at least \$500,000 and ignored the large number of cases where a contract pays out a total over \$500,000 in several increments. Our analysis found that correction of this flaw in the administration's analysis increases the estimated number of affected contractors to at least 50,348 and possibly as many as 88,612.
5. Added initial cost for setting up system to compile and track company's own labor law violations across all establishments and Federal and State jurisdictions, including information systems development and staff training. Interviews of large and small contractors results in an average of \$12,000 per company. Multiplied by 50,348 affected contractors yields \$600 million of costs not accounted for by the administration.
6. Added initial cost for design, development and implementation of system to compile and track labor law compliance information of subcontractors. Interviews with large and small contractors yield an average of \$18,000 per prime contractor. Multiplied by 50,348 affected contractors yields \$900 million in costs not accounted for by the administration. [Note: 50,348 affected contracts is based on identified prime contractors. This does not include the many tiers of subcontractors who will have to evaluate lower tier subcontractors under the proposed regulation.]

The Administration's estimate of subsequent year on-going costs of \$92 million increases to \$3 billion per year based on items 1 – 4 above. While items 5 and 6 above are first year costs only, experienced contract managers interviewed noted that there would be additional annual on-

going costs for maintaining, auditing and employee turnover training related to the systems described by items 5 and 6, which have not been explicitly estimated or added to the cost estimate shown.

If the higher range of compliance activity labor time estimates reported by interviewees (6 x administration's values) and a higher estimate of the number of affected contractors described above (88,612,) is applied, the on-going annual cost increases to \$6.6 billion. Additionally, if the one-time cost per company for designing, developing and implementing a compliance information system for tracking its own labor compliance issues is increased to \$15,000 (a distinct possibility given uncertainty and complexity) and the per company amount for the subcontractor tracking system development is increased to \$25,000 (a distinct possibility due to uncertainty and complexity), the first year compliance costs escalate to \$11.4 billion.

In addition, on-going compliance costs would also include costs for the following items, which while foreseeable, are not quantifiable at this time. This list is illustrative, not exhaustive.

1. The increases in award protests that will occur. Interviewees estimated the outside legal counsel cost of the typical protest at \$150,000 per client. Double this to \$300,000 for both sides of the protest. If the number of additional protests is 1,500 (a 50% increase over the current annual number that experts believe is likely), the additional annual compliance cost would be at least \$450 million. If the rule causes a doubling of protests, the amount would be \$900 million. These are amounts only for the outside counsel costs. The opportunity cost of time of each company's own staff and of government contract officer staff would result in a greater cost impact.
2. In addition to the contractor staff time for preparing and submitting supplemental materials regarding reportable labor compliance administrative determinations, most contractors will also incur costs for outside counsel to advise, assist, and review materials before submission during the bidding process. The total cost impact will depend on the proportion of affected contractors who use outside counsel for this purpose, which is data that needs to be obtained to add this item to the aggregate cost estimate.
3. Delays in the procurement process because of the burden of submitting and evaluating supplemental information required by this regulation. These delays will impact scheduling of work and will result in higher charges for completing tasks on a rush basis.
4. Litigation costs and delays related to the role that the regulation will impose on prime contractors to evaluate the labor compliance records of subcontractors; prime contractors will be exposed to "disparagement" lawsuits seeking damages by prospective subcontractors who are not chosen to join a bid because of the prime's evaluation.
5. Costs and uncertainties that this regulation adds to the procurement process will discourage companies from bidding for Federal contracts, reducing competition and leading to higher costs for government support services. Particularly hard hit will be small contractors who will not have the resources to absorb the complexities and burdens of this E.O. and regulations.

6. Increased litigation costs and incidence resulting from the prohibition in the proposed rule on using pre-dispute arbitration agreements for contracts over \$1million. The administration's regulatory impact analysis identified this as a notable cost element, but did not extend the analysis to the point of making an aggregate cost estimate. This is an area where further research and analysis effort is needed.
7. The impact of all the tracking and reporting requirements involving the "equivalent state laws" is unknowable since there has been no guidance on what constitutes these laws. However, there is no question that the costs associated with this requirement will be substantial and the process cumbersome and complex.