ACEC
AMERICAN COUNCIL OF ENGINEERING COMPANIES
of Ohio

February 11, 2011

Elaine Roberts, AAE
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Dear Elaine:

Thank you for the opportunity to review the Columbus Regional Airport Authority's *Audit Guide for Consulting Services Cost Rates,* dated January 1, 2011. We are cognizant and appreciative of your responsibility to procure architectural and engineering services in a cost-effective manner, and we appreciate your efforts to set out clearly the policies and procedures that will guide the Authority's review of consultant fee proposals and overhead rates.

Upon its receipt, we shared the draft guide with ACEC members, both in Ohio and outside the state, and with consultants upon whom the industry relies for their expertise relating to Part 31 of the Federal Acquisition Regulation (FAR), which sets the criteria for determining costs eligible for reimbursement on federally funded A/E contracts.

Based on the feedback we received from these various sources, our comments and recommendations are as follows:

Sec. 1. (b.) – While the guide states that, "it is our fiscal responsibility to ensure the fees we pay for consulting services are reasonable in comparison to similar projects at other airports," no other major airport with which our members have done business imposes the kinds of non-FAR-based limitations on indirect costs such as those set out in the audit guide. We will expand on this observation below.

Sec. 2. (b.) – The guide states that CRAA maintains an audit group to "ensure that funds paid to outside organizations are FAR eligible," yet the Authority does not accept overhead rate audits conducted in conformance with the FAR and approved by other federal or state "cognizant" agencies. Moreover, the guide proposes to exclude overhead costs that are *specifically allowable* under the FAR.

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Sec. 3. (a.)(x.) – Representatives of a firm selected for contract negotiation must be prepared to meet with the CRAA negotiation team within five days of notification of selection. Given that the firm's financial personnel may be located in an office in another state, ACEC Ohio recommends that the Authority consider conducting this meeting by video conference or telephone conference whenever practicable.

Sec. 3. (a.)(x.)(i.) – ACEC Ohio supports the goal of expediting the contract negotiation process. However, we are concerned that a firm selected for contract negotiation could be unable to meet the five-day deadline if the Authority requires the submission of substantial information beyond that contained in the firm's FAR audit. We suggest that 10 days be allowed for submission of such additional information.

Sec. 3. (a.)(xiv.) – The final sentence of this section seems to imply that the Authority may conduct a post-contract audit for an unlimited period of time following contract completion. The contract should always specify a reasonable time limit for the conduct of post-contract audits, after which the consultant should not expected to maintain or produce relevant financial records.

Sec. 4. (b.) – Again, as observed above, five days is an extremely short time period for the preparation, gathering and submission of the volume of financial information requested. We believe 10 days is more appropriate.

Sec. 4. (c.)(i.)(1.) – We strongly disagree with the Authority's decision to exclude bonuses from overhead, which apparently is based on the mistaken belief, expressed in Sec. 7. (e.) (i.) that bonus payments "essentially reflect a distribution of profits." FAR Part 31 makes a clear distinction between bonuses and distributions of profit, and outlines requirements for allowability.

Compensation paid via bonus is clearly allowable under Federal Acquisition Regulation 31.205-6 (f)(1), provided that:

> (i) Awards are paid or accrued under an agreement entered into in good faith between the contractor and the employees before the services are rendered or pursuant to an established plan or policy followed by the contractor so consistently as to imply, in effect, an agreement to make such payment; and
>
> (ii) Basis for the award is supported.

Further, FAR 31.205-6 (a)(6) provides that for owners of closely held firms, allowable bonus amounts *may not* represent a distribution of profits.

Bonus plans are an essential and cost-efficient component of the compensation system of many A/E firms. Those firms that compensate employees through a combination of salary and bonus have the ability to adapt to rapidly changing business conditions.

In an economic downturn, firms that compensate through salary alone have little choice but to use layoffs to reduce compensation costs. Conversely, firms that compensate through a combination of salary and performance-based bonuses can reduce those bonuses during difficult economic conditions, limiting the effect of staff reductions and thereby reducing the expensive process of hiring and training new personnel when business conditions improve.

Accordingly, we strongly believe that bonus payments paid in compliance with the FAR should be permitted as a component of A/E firm overhead rates. No other major airport of which we are aware has imposed such a limitation on this legitimate item of overhead, and given that certain bonus payments are clearly allowable under the FAR we urge the Authority to revisit its policy in this area.

Sec. 4 (c.)(i.)(3.) – In our meeting of December 16, 2010 and in your letter of December 30, 2010, it was stated that the Authority would not look favorably upon any firm productivity rate of less than 57%, a threshold based on data produced by a recent Zweig White survey. This section now states that the Authority's required rate has been increased to 60%.

While it is true that a firm's productivity or utilization rate does have a significant effect on the overhead rate, there is no basis in FAR to apply such a limitation. A review of Zweig White and PSMJ financial performance surveys indicates that even in years of economic expansion, the average productivity rates hover around 60%. In recent years, due to the severe economic downturn, those surveys reflect that the average rate has declined several percentage points, and for this reason we believe that, if such a limitation must be applied, the original 57% productivity rate is the more equitable threshold. However, we urge the Authority to consider amending the guide to comply with the FAR requirements for reasonableness of total compensation, rather than focusing on the firm's productivity rate.

Sec. 4. (c.)(iii.) – This section provides that for projects in excess of $300,000, where the consultant's overhead exceeds 140%, the Authority will perform a "more extensive review." Please explain what would be involved in such a review. Specifically, are there other limitations or financial measures (e.g., rent and utilities, international lines of business, insurance, payroll taxes, etc.) that would be applied to further adjust the firm's overhead rate?

Will CRAA continue to use Zweig-White or other survey data as benchmarks in reviewing other components of overhead besides staff productivity? We hope this will not be the case. The basis of the Z-W survey metrics do not include data relevant to large firms and we believe they should not be used as the basis for evaluating rates. If CRAA will continue this practice for projects in excess of $300,000, we recommend this be made very clear in the audit guide so that firms have a good understanding of what is expected in the negotiation process.

Sec. 5. (e.)(I.)(A.)(3.)(b.)(1.) – This section provides for the adjustment of wage rates only after 12 months under contract. However, most ACEC member companies conduct performance and salary reviews toward the end of each calendar year, which means that on agreements negotiated late in the year, firms are locked into below-market wage rates that erode the profit margin of the project. This penalty is multiplied in multi-year contracts. Some provision should be made to allow for ongoing adjustment in wage rates as these rates are adjusted by the firm.

Sec. 5. (e.)(I.)(B.)(1.) – This section provides that submission of an overhead rate of 140% or higher triggers the requirement that the firm submit substantial additional financial information, even when the firm has an approved overhead rate established as the result of a FAR audit. We also note that the average overhead rate for Ohio firms is approximately 156% and has been within a range of 154% to 161% for the past five years.

Certainly any firm that does not have a current FAR audit should be required to document its proposed overhead rate. However, we believe that when a firm has a FAR-compliant overhead rate that exceeds 140%, the "additional review" provided for in the guide is superfluous and places an unnecessary and costly burden on both the Authority and the firm.

Indeed, such additional review – and the significant cost involved – would be unnecessary if the Authority were to accept FAR-compliant audited overhead rates and discontinue the practice of disallowing overhead costs that are allowable under current federal regulations.

Sec. 5. (e.)(I.)(C.)(2.) – The 8% profit rate is generally low, especially given that the Authority also intends to restrict overhead rates to well below what is permitted under the FAR. The Ohio Department of Transportation permits an 11% profit rate while the City of Columbus allows 10%, and their projects generally are less complex than CRAA projects.

To summarize, we believe the restrictions on overhead costs set out in this guide – restrictions that do not comply with the requirements established in the Federal Acquisition Regulation – are not in the best interest of our member firms. Moreover, we believe these restrictions are not in the best long-term interest of the Authority.

While economic conditions remain difficult, the Authority may see no diminution of interest in its projects, even despite the cost limitations set out in the guide. When conditions improve, however, we believe many firms will conclude it makes no sense to compete for CRAA design projects if they cannot recover their legitimate overhead costs and earn a fair profit.

In the surface transportation arena, federal and state authorities are placing greater emphasis than ever before on the importance of auditing design firms to ensure their overhead rates are established in accordance with federal guidelines and cost limitations. Such authorities have established a uniform interpretation of the FAR in the AASHTO *Uniform Audit & Accounting Guide*, to be used by federal, state and local agencies. The federal government also is requiring state and local agencies to accept "cognizant" audits that are performed in jurisdictions other than their own, providing such audits are FAR-compliant, specifically to eliminate the cost of redundant audits.

While airports are not currently required under federal law to accept cognizant audits, FAA Advisory Circular 150/5100-14D requires costs incurred to be consistent with the FAR cost principles detailed in 48 CFR Part 31. Accordingly, we propose that the Authority adopt a policy requiring FAR compliance and providing for the Authority's acceptance of cognizant audits. Doing so would ensure that consultants with whom the Authority contracts are in compliance with federal restrictions on overhead costs, and would greatly reduce the time invested by the Authority's staff in conducting unnecessary reviews of consultant financial information.

Thank you for the opportunity to review the audit guide and for your consideration of our comments and recommendations.

Sincerely,

Don Mader

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Executive Director

DLM:mc

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