

# Port of Seattle Audit Committee – Special Session

## *Architectural & Engineering Consultant Rates*

February 11, 2020

Pier 69, Commission Chambers

9:00 AM – 10:00 AM

# Architectural & Engineering Consultant Rates

- Architectural and Engineering costs account for approximately 10-20 percent of capital costs
- \$3.6 billion in capital spending over the next five years
- RCW 39.80.050 states “The agency shall negotiate a contract with the most qualified firm...at a price which the agency determines is fair and reasonable”

# Washington State Auditor's Office

## (Columbia River Crossing Project – April 2014)

- “...industry sources indicate you must know a firm’s overhead rate to know the profit markups you are paying...”
- “...most state transportation departments typically pay a **10 percent to 12 percent** consultant markup on labor and overhead.”
- “...the American Council of Engineering Companies (ACEC), helped develop a WSDOT policy that would directly benefit larger firms that engage sub-consultants to perform work for the state agency.”

# Industry Standards / Benchmarks

- 23 CFR Part 172, “Fixed fees in excess of **15 percent** of the total direct labor and indirect costs of the contract may be justified only when exceptional circumstances exist.”
- Benchmarked with several airports and local governments.

# IA approach to determining consultant markup

- Obtained direct labor for 407 consultants (8 contracts / 33 firms)
- Consultant Markup = Negotiated Rate – (Direct Labor + Indirect Cost\*)

Example:

Negotiated Rate: \$160.00

Direct Labor: \$48.47

Overhead: 136.92% (\$66.37)

Calculation:  $\$160 - (\$48.47 + \$66.37) = \$45.16$  (39.3%)

\* Approved FAR 48 CFR Part 31 audited overhead rate, WSDOT overhead rate, or WSDOT Safe Harbor rate.

\* 15 of the 33 firms did not provide an approved audited overhead rate; accordingly we used WSDOT's Safe Harbor rate for those firms.

➤ CPO had not established guidelines for what is determined fair and reasonable. Our testing of over 400 A&E consultants identified many instances where profit margins exceeded what the industry deemed reasonable.

✓ Below table reflects the profit margins of the firms tested: *[Note: Industry standard ranges between 10 – 15 percent.]*

<b>Profit</b>	<b>10% and below</b>	<b>11-19%</b>	<b>20-29%</b>	<b>30-39%</b>	<b>40-49%</b>	<b>Above 50%</b>
<b>Number of Consultants</b>	139	81	79	60	30	18

34%

66%

➤ Management approval was not required when hourly rates exceeded the maximum rates produced by the service rate negotiation tool/model.

- ✓ Tool developed by BCG and uses market data to produce a target\* and max rate.
- ✓ 10 contracts and 693 position reviewed.
- ✓ Below table reflects the number of positions that exceeded the maximum and the amount that the Port agreed to pay over the maximum rate for every hour worked:

<b>Positions</b>	<b>Amount over the Maximum (+2%)</b>
<b>31</b>	<b>\$51.05 - \$175.03</b>
<b>32</b>	<b>\$21.20 - \$48.05</b>
<b>103</b>	<b>\$.17 - \$19.98</b>
<b>166</b>	

166 / 693 = 24%

\* When we looked at positions that exceeded the BCG Model's target rate, our testing indicated that 487/693 or 70% of the positions exceeded the model's target rate.

# Recommendations

- The Procurement Council should determine what the Port deems a fair and reasonable rate and should document the rationale for transparency.
- CPO should engage a third party to perform an independent model validation of the rate tool, so that management can gain confidence that the model produces accurate market rates.



# Recommendations

- CPO should implement a management review process when consultant rates exceed the maximum. This review should be documented and contain established criteria and approval thresholds (i.e., up to 20% over the maximum) for both the Services Agreement Manager and Planning and Analytics Manager to approve.
- If the thresholds exceed their authority or if agreement cannot be reached, approval should be escalated to the appropriate person (i.e., director, COO) for approval, as required by the authority guidelines.

➤ A reconciliation between the final negotiated rates and the contract did not occur. As a result, we were unable to verify that all positions and rates reflected in the contract were accurate.

- ✓ 10 contracts reviewed, for 817 positions.
- ✓ Below table reflects the type and number of exceptions:

Position on contract did not exist on the rate tool	108
Rate on rate tool did not agree to the contract	40
Position on rate tool did not exist on the contract	20
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	168

817 = 21%

# Recommendations

- CPO should retain documentation to evidence the agreed upon rate and position.
- CPO should the use this documentation, to verify that the rates are accurately captured into the contract before it is executed.

- The Central Procurement Office is responsible for procuring all contracts related to public works, consulting services, and goods and services. Governance meetings, for Executive Leadership Team (ELT) oversight of CPO, had not occurred since December 7, 2017.

*“...the establishment of the Procurement Council and its ELT-level membership from across the Port signals the fundamentally cross-functional nature of procurement. This group has and will continue to serve as a ‘leadership by example’ in terms of overcoming silos and operating as ‘One Port’.”*

*“Procurement will continue to be guided and overseen by the Procurement Council, a group of ELT-level stakeholders. This body will continue to meet beyond our engagement with BCG and will be a core aspect of Procurement Excellence into 2017 and beyond.”*

*“Continued leadership and management commitment, as demonstrated by ongoing engagement in the Procurement Council, and more importantly, by each leader holding their respective teams accountable for engaging proactively and constructively with CPO.”*

# Recommendations

- The Chief Operating Officer should lead an effort to determine the meeting frequency and information that is deemed necessary to perform effective governance.
- We also recommend that, at a minimum, the CFO and the Port's Managing Directors of Aviation and Maritime, attend these meetings.
- Finally, we recommend developing a charter that defines the purpose, objective, and voting rights (if necessary) within the Governance Committee.