

RESPONDING TO REQUESTS FOR DISCOUNTS OR UNILATERAL FEE REDUCTIONS

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Tough Times Breed Drastic Measures ...

- ❑ CIP and agency budgets have seen massive cuts
- ❑ Falling revenues and bond funds prompt agencies to seek “creative” means to stretch budgets
- ❑ State and local agencies have asked for “voluntary” reductions in billings on existing contracts
- ❑ Some go even further—imposing unilateral reductions in fees paid to consultants
- ❑ These agencies claim the savings will be used to retain key staff or support other projects

And Problems For Private Consultants

- ❑ Consultants feel pressured to accept these discounts or risk negative evaluations or even black-listing
- ❑ Some firms decide cuts are lesser of two evils if they preserve long-term relationships
- ❑ Discounts undercut QBS principles requiring negotiation of terms and fees for services
- ❑ Consultants suffer twice—they are paid less and they get no reduction in contract scope or their liability
- ❑ Discounting agreed fees erodes (already limited) profit potential on government contracts
- ❑ For smaller firms, discounts often threaten their survival

Which Agencies Are Doing This?

- No reports of federal government doing so— underpayments must be justified, documented, and the contract scope equitably adjusted
- State and local government, including transportation departments, engineering and public works departments are requesting discounts
- Word that public agencies are requesting discounts often spurs private developers to do the same

Can The Owner Reduce Your Fee?

- ❑ Owner usually cannot modify a signed contract to pay less for same scope of services
- ❑ Must either reduce scope or terminate for convenience to avoid paying fees otherwise due
- ❑ Offering to pay less than previously agreed for same services is unenforceable “naked” promise
- ❑ But, if Consultant voluntarily bills less than the contract fee, Owner can accept the discount
- ❑ Q: How do Owner and Consultant account for unbilled fees and re-allocation of funds?

Unilateral Reductions Are Risky

- FHWA disapproved state DOT reduction of fees on existing contracts funded with federal aid, finding:
 - Brooks Act (40 USC §1101-1104) requires QBS and good faith negotiations with consultant on scope, fee and terms
 - Federal-Aid Highway Program incorporates Brooks Act (23 USC §112(b)(2)(A)) for award of design and engineering contracts
 - State DOT must adopt written contracting procedures approved by FHWA for selection of engineering consultants (23 CFR 172.9(a))
 - State DOT did not obtain FHWA approval to consider budget constraints as basis for altering contracts, or to modify contracts without negotiation
 - Federal funds may not be used unless costs are incurred in conformity with applicable federal law or regulations (23 CFR 1.9(a))
- FHWA required negotiated reductions in scope to match fee, and federal approval of state's future plans for revising consultant's contracts on Federal Major Projects

Accounting For Fee Discounts

- Discounts present accounting problems for both the Consultant and the Owner:
 - Will the invoiced amount be reduced by a percentage?
 - For cost-reimbursable contracts, will consultant bill less hours than actually charged to the project?
 - Will non-billable hours be charged off to overhead?
 - What impact will discounts have on audited overhead rates?
 - How will owner reduce final contract balance for portion not billed?
 - How will owner account for re-allocation of funding?
 - Consultants must pay their staff for all hours worked, regardless of whether those charges are billed

Is Promise To Discount Fees Charged On An Existing Contract Binding?

- Generally, under state law principles:
 - ▣ A promise to pay (less) given after services are performed or other benefit provided is not enforceable. *Restatement (Second) Contracts §71*; 4 Williston on Contracts §8:11 (4th ed.)
 - ▣ But, modification of existing contract is binding if “fair and equitable in view of circumstances not anticipated by the parties when the contract was made....” *Restatement (Second) Contracts §89(a)*
 - ▣ One party who has performed contractual duties may agree to discharge the other party from its obligation to perform part or all of its agreed duty *Restatement (Second) Contracts §275*

Is Request For, Or Offer of, a Discount or “Free Services” Ethical?

- ❑ Consulting engineers and other design professionals must be certain they understand what their client wants, and (if possible) where the unpaid funds will be used.
- ❑ If funds are diverted to the personal benefit of the client’s staff or administrators, or some other unauthorized use, it may create the appearance of a bribe or illegal gratuity.
- ❑ Such conduct may be unethical

AIA 2007 Code of Ethics & Professional Conduct

Rule 2.101: *Members shall not, in the conduct of their professional practice, knowingly violate the law.*

Rule 2.102: *Members shall neither offer nor make any payment or gift to a public official with the intent of influencing the official's judgment in connection with an existing or prospective project in which the Members are interested.*

ASCE Code of Ethics

Canon 6: *Engineers shall act in such a manner as to uphold and enhance the honor, integrity, and dignity of the engineering profession and shall act with zero tolerance for bribery, fraud, and corruption*

- a. Engineers shall not knowingly engage in business or professional practices of a fraudulent, dishonest or unethical nature*
- c. Engineers shall act with zero-tolerance for bribery, fraud, and corruption in all engineering and construction activities in which they are engaged*
- d. Engineers should be especially vigilant to maintain appropriate ethical behavior where payments of gratuities or bribes are institutionalized practices*
- e. Engineers should strive for transparency in the procurement and execution of projects [...]*

NSPE Code of Ethics For Engineers

Fundamental Canon 6: *Engineers, in the fulfillment of their professional duties, shall conduct themselves honorably, responsibly, ethically, and lawfully so as to enhance the honor, reputation, and usefulness of the profession*

Rules of Practice 5: *Engineers shall avoid deceptive acts:*

b. Engineers shall not offer, give, solicit, or receive, either directly or indirectly any contribution to influence the award of a contract by public authority, or which may be reasonably construed by the public as having the effect or intent of influencing the awarding of a contract. They shall not offer any gift or other valuable consideration in order to secure work

FAR Contractor Code of Business Ethics and Conduct

FAR Subpart 3.10, Part 3.1003(a)(2): Whether or not the clause at 52.203-13 is applicable, a contractor may be suspended and/or debarred for knowing failure by a principal to timely disclose to the Government, in connection with the award, performance, or closeout of a Government contract performed by the contractor or a subcontract awarded thereunder, credible evidence of a violation of Federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations found in Title 18 of the United States Code or a violation of the civil False Claims Act. Knowing failure to timely disclose credible evidence of any of the above violations remains a cause for suspension and/or debarment until 3 years after final payment on a contract

(FAR Clause 52.203-13 used if contract value >\$5M and duration ≥ 120 days)

Discounts Violate QBS Principles

- Federal Brooks Act, 40+ jurisdictions with mini-Brooks Acts, and states/municipalities adopting the ABA Model Procurement Code For State and Local Government require QBS procedures for selection of design professionals and negotiation of contracts

“The policy of the Federal Government is to publicly announce all requirements for architectural and engineering services and to negotiate contracts ... on the basis of demonstrated competence and qualification for the type of professional services required and at fair and reasonable prices.” 40 USC §1101

Arizona QBS Mirrors Brooks Act

A.R.S. §34-103.F

[T]he agent shall enter into negotiations with the highest qualified person or firm on each final list or, in the case of a final list for multiple contracts to be awarded to separate persons or firms, the agent shall enter into negotiations with a number of the highest qualified persons or firms on a final list equal to the number of contracts that may or will be awarded. The negotiations shall include consideration of compensation and other contract terms that the agent determines to be fair and reasonable to the agent. In making this determination, the agent shall take into account the estimated value, the scope, the complexity and the nature of the professional services to be rendered.

Arizona QBS Discourages Discounts

A.R.S. §41-2538.E

The award shall be made to the offeror determined in writing by the head of the purchasing agency or a designee of such officer to be best qualified based on the evaluation factors set forth in the request for proposals and **after a written determination that the compensation is fair and reasonable.** Selection may be made pursuant to the provisions of this section without requiring priced proposals, but if price is included in proposals submitted, **no contract may be awarded solely on the basis of price.**

Could Discounts Trigger FAR Price Reduction Clause?

A: Not certain.

FAR Paragraph 5.402: Contracting officers must (a) purchase supplies and services from responsible sources at fair and reasonable prices.

FAR Paragraph 15.408(b): The Contracting officer shall, when contracting by negotiation, insert the clause at 52.215-10, Price Reduction for Defective Cost or Pricing Data, in solicitations and contract when it is contemplated that cost or pricing data will be required from the contractor or any subcontractor.

FAR Clause 52-215-10(a): If any price, including profit or fee, negotiated in connection with this contract, or any cost reimbursable under this contract, was increased by any significant amount because—

(1) The Contractor or a subcontractor furnished cost or pricing data that were not complete, accurate, and current as certified in its Certificate of Current Cost or Pricing Data;

Talking Points On Discount Requests

1. Fee negotiation should occur before contract is signed
2. Fee discount violates Brooks Act
 - a. Denies A/E “fair and reasonable” fee
 - b. No negotiation
 - c. No corresponding reduction in scope or terms
3. Underpayment for services violates terms of federal aid and approved program requirements
4. Diversion of funds from approved purpose could violate state or federal false claims acts
5. Soliciting or giving discounts violates ASCE/NSPE Code of Ethics
6. Greater savings achieved by postponing or cancelling other projects—saving both design and construction cost
7. Proper means to reduce fee is deductive change order with reduced scope or termination for convenience
8. Inequitable to reduce fee without reducing scope or liability exposure
9. Fear of favor or retribution indicates request for voluntary discount is unethical on part of agency.

Making A Record On Discounts Given

If your firm agrees to give a discount:

1. Have client's CO or agency head put request for discount in writing
2. Request confirmation that client has legal authority to discount payments, including governing board resolution or determination
3. Consider asking client to identify use to which retained funds will be applied (May be better not to ask, and not to know)
4. Request a deductive change order to reduce contract value
5. Do not bill full amount and remit difference back to client
6. If possible, request a written opinion from agency IG, ethics officer, or legal counsel that fee discount and fund transfer is legal and ethical
7. Document chargeable hours properly and pay employees full value of their services (unhappy employees are future whistleblowers)
8. Do not prepare, sign, or certify any document, report, invoice, or other item that falsely, inaccurately, or incompletely describes and accounts for discounts taken

Your Speaker



With thirty years experience in design and construction law, **P. Douglas Folk** has been an advocate for design professionals and contractors in professional liability and construction defect claims, contract disputes, and disciplinary proceedings. Doug serves on Arizona's Board of Technical Registration by governor's appointment. He is a member and past chairman of ACEC's Legal Counsels Forum, a member of the ACEC Risk Management Committee, past chairman of the State Bar of Arizona Construction Law Section, and co-editor of *Design Professional and Construction Manager Law* published by the American Bar Association. Doug Folk is recognized in the 2010-2011 editions of *Best Lawyers in America*® for Construction Law and *Arizona Super Lawyers*® for Construction Litigation and Professional Liability Defense.

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