



# THE AMERICAN INSTITUTE OF ARCHITECTS

STATEMENT OF  
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***“Reform Procurement Rules That Delay  
Government Payments to Small Architecture and  
Engineering Firms”***

United States House of Representatives  
Committee on Small Business  
Subcommittee on Regulations, Healthcare & Trade

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Mr. Chairman, Ranking Member Westmoreland, and members of the Subcommittee — good morning. I am Paul Renker, an architect, small business owner, and member of the American Institute of Architects. Since nearly half of the AIA’s members own or work for small firms, we appreciate the work that this Committee does for small businesses.

Thank you for inviting me to discuss two federal procurement regulations that have been identified under the Small Business Administration’s (SBA) r3 Initiative as being burdensome on small businesses that contract with the federal government: retainage for architectural and engineering services and reverse auctions.

Commonly referred to as the “retainage clause,” the Federal Acquisition Regulation (FAR) rule for fixed-price architectural-engineering services ([48 CFR 52.232-10](#)) allows federal agencies to impose a 10-percent withholding, or retainage, on fees for firms providing architectural and engineering services. This rule allows federal contracting officers to withhold 10 percent of the amount owed to A/E firms under the contract until the full construction of a project is complete. The 10-percent withholding for design services is out of line with other federal contract payment regulations, which typically have no withholding fee or a maximum of a five percent withholding.

Earlier this year, as part of the SBA’s r3 initiative, the SBA identified the 10-percent retainage clause as one of the Top 10 federal rules in need of reform. This retainage

clause presents an unnecessary burden to nearly 230,000 small A/E firms<sup>1</sup> who contract with the federal government. This is a strong deterrent for those small firms wishing to pursue federal contracts for three reasons.

First, 10 percent is higher than the amount withheld under many other types of service contracts. As the Administrator of the Council on Federal Procurement of Architectural and Engineering Services (COFPAES), of which the AIA is a member, recently testified before this Committee, “10 percent withholding for design services is ... out of line with other federal contract payment regulations which typically have no withholding fee or a maximum of a five percent withholding.”<sup>2</sup> For small design firms with very small profit margins and tight cash flows, having 10 percent (or greater) of their fee held back for what could be years is very troubling. The withholding restricts the cash flow of small businesses and in some instances is in addition to any insurance requirements that may be imposed.

Second, A/E firms typically complete the major portion of their work (the design phase of a contract) long before construction is complete, leaving the architectural firm short of 10 percent of the payment amount for a substantial period. The result, as the Chairman of

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<sup>1</sup> Small Business Administration Regulatory Review and Reform Initiative Regulatory Review and Reform (r3) Top 10 Rules, 2008- [http://www.sba.gov/advo/r3/r3\\_services08.html#se](http://www.sba.gov/advo/r3/r3_services08.html#se)

<sup>2</sup> Testimony of John M. Palatiello, Administrator, Council on Federal Procurement of Architectural & Engineering Services before the House Committee on Small Business (March 6, 2008).

the American Council of Engineering Companies Small Firms Council recently said, is “an interest free loan to the federal agencies at small firms’ expense.”<sup>3</sup>

Third, a 10-percent retainage requirement is not necessary in order to protect taxpayers. There are common methods of determining whether performance of architectural services has been satisfactory long before payment for services or completion of construction. Furthermore, the withholding is counter to the Brooks Act (Public Law 92-582), which established the qualifications-based selection (QBS) process for A/E firms. The QBS process ensures that only the most competent and capable firms – those with a proven track record of good performance – are selected for design contracts with federal agencies, even before they negotiate potential fees.

The 10-percent withholding rule is causing significant financial hardships on small A/E firms contracting with the federal government. I would like to take a few moments to relate our firm’s first experience with a federal project.

Through the QBS process our firm was chosen and awarded a contract to design a new Job Corps Center for the U.S. Department of Labor in St. Petersburg, FL. This was a small business award, and we are very proud and happy to have been selected.

We started fee negotiations at the beginning of June 2006. We completed fee negotiation and received our notice to proceed approximately 115 days later on September 25, 2006.

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<sup>3</sup> Submission of the Chief Counsel, Office of Advocacy, Small Business Administration, to the Office of Management and Budget, March 13, 2008.

We received our first payment for services approximately 105 days after our notice to proceed, or approximately 220 days from the start of fee negotiations. I mention this because our firm, as a small business, has to staff and plan for large projects such as this. This resulted in our firm incurring costs and expenses for salaries and overhead for 220 days without compensation. Our firm was forced to borrow money to maintain salaries and expenses. When compensation was received, 10 percent was withheld, further impacting our cash flow.

We understand that the intent of the 10-percent retainage is to protect the government and taxpayers, to help ensure they receive services equal to or greater than for services paid. However, this is not required under the system under which architects and engineers provide services.

In our case the Department of Labor contract includes a handbook and detailed descriptions of services and deliverables required for payment. We are required to submit progress documentation of our work at 15-percent, 30-percent, 60-percent and 100-percent milestones. In each case we submit our progress documents to other professionals hired by the Department of Labor. These professionals review our work in great detail for compliance with submittal requirements as well as compliance with the design program intent. Only after our submittal is reviewed and approved by the Department of Labor is our Invoice for Services accepted and processed for payment. Once our invoice is accepted, payment is normally made electronically in 30 days. But payment from completion of our work at each submittal was actually 43 days at the 15-

percent submittal, 46 days at the 30-percent submittal, 49 days at the 60-percent submittal and 76 days at the 100-percent submittal. As you can see there are already very strong safeguards in place to protect the government and taxpayers without the additional burden of the 10-percent retainage.

The 10-percent retainage of our fees was held in increasing amounts over the entire period of design services. After the project was successfully bid we were told that we could write a letter requesting the Department of Labor release our retainage for design services. We received our 10 percent retainage, without interest, approximately 500 days (one year and four-and-a-half months) after our contract notice to proceed.

The 10-percent retainage was started again during construction administration services and to the best of my knowledge will continue for the full duration of construction, or approximately for 527 days. It should also be noted that 10 percent is not retained from the contractor's pay requests.

When this rule was incorporated into the FAR in 1984, the FAR council included a clause that would allow the release of the withheld funds when the design services (the A/E firms' portion of the work) have been satisfactorily completed.<sup>4</sup> In recent years, however, many A/E firms have reported that, as in our case, contracting officers continue to withhold the 10-percent until full construction of the project is complete.

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<sup>4</sup> 48 C.F.R. 52.232-10 - "payment may be made in full during any months in which the Contracting Officer determines that performance has been satisfactory."

As noted previously, the SBA has listed the 10-percent retainage requirement for A/E contracts as one of the top ten federal rules for review and potential reform, saying that a “change in this regulation will help increase the cash flow of small A&E firms that contract with the federal government. This change should also encourage more firms to enter the federal procurement market, with concomitant improvements in the quality of services.”<sup>5</sup> As the Small Business Committee is dedicated to opening the federal marketplace to small businesses, we strongly encourage Congress to fix this burdensome regulation.

In order to level the procurement playing field, Congress should eliminate the retainage requirement and take steps to ensure that contracting officers make full payment when the design services themselves have been satisfactorily performed rather than when the entire construction project is complete. This will ensure that small A/E firms are able to pursue work with the federal government without placing their businesses’ financial stability on the line.

Another issue on the SBA’s r3 agenda is reverse auctioning. According to the SBA:

*In the federal government’s procurement system, the live electronic reverse auction technique was designed as a contracting tool to provide contracting officers with flexibility to make contract awards in a timely manner. Bidders who use the technique submit their bids through an online intermediary and are*

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<sup>5</sup> Small Business Administration, Office of Advocacy, “Small Business Regulatory Review and Reform Initiative, Regulatory Review and Reform (r3) Top 10 Rules, 2008.”

*informed of competitors' prices but not their identity. Bidders offer successively lower prices until no lower price is offered. The agency must then decide whether it will make the award. Some current techniques used by contracting officers may have the unintended result of circumventing Federal Acquisition Regulation (FAR) Part 19, which requires agencies to set aside certain dollar threshold contracts for small businesses. The problem exists because no specific FAR regulation instructs contracting officers in how to use the reverse auction tool.<sup>6</sup>*

The Office of Advocacy has recommended development of rules that continue to provide contracting officers with the flexibility of reverse auctions while not conflicting with FAR Part 19 small business competition requirements.

The AIA and most other construction entities view reverse auctions as a dangerous concept that induces bidders, in their efforts to be the lowest bidder, to reduce labor and supervision to levels that could endanger safety and lessen quality. In fact, we believe that reverse auctions violate the qualifications-based selection procedures outlined under the Brooks Act (Public Law 92-582) and FAR Part 36.6. Architects and engineers provide a unique service and are not commodities. Because of this, their services cannot be procured in the same manner as office supplies, computers or automobiles, where there is a standard benchmark to compare the products being bid on.

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<sup>6</sup> SBA Office of Advocacy, [http://www.sba.gov/advo/r3/r3\\_auction08.html#au](http://www.sba.gov/advo/r3/r3_auction08.html#au)

In summary, rules like the ten percent retainage and reverse auctions present considerable roadblocks to small and emerging A/E firms that want to help design and build the buildings that are literally symbols of our nation's vitality, stability and grandeur. We hope that as this Subcommittee continues to explore ways of ensuring that federal procurement laws and regulations provide ample opportunities for small businesses to compete, it also recognizes the unique role that architects and engineers play in ensuring the health, safety and welfare of the millions of people to work in and visit federal facilities every year.

Thank you, Mr. Chairman and members of the Subcommittee, for giving me the opportunity to testify today. I will be pleased to answer any questions you may have.