

**Arkansas State Highway & Transportation Department**  
**Indirect Cost Rate Audit Requirements**

## **Executive Summary**

### *Necessity*

This document replaces the *Indirect Cost Rate Audit Requirements* of the Arkansas State Highway and Transportation Department (hereinafter referred to as the Department) as issued on February 22, 2002. This document is designed to address the requirements for overhead audits as outlined in the AASHTO *Uniform Audit & Accounting Guide for Architectural and Engineering (A/E) Consulting Firms* 2010 Edition.

All firms will be required to provide an audit of the firm's indirect cost (overhead) rate for the most recent fiscal year ended. The audit must be performed by an independent Certified Public Accountant (CPA) or cognizant government agency in accordance with *Government Auditing Standards*. An electronic copy of the *Government Auditing Standards* is available on the U.S. Government Accountability Office website at this link: <http://www.gao.gov/govaud/ybk01.htm>. Firms whose audits have been conducted by an independent CPA are also required to submit a letter of cognizant approval from a cognizant State or Federal Agency in their home State if available.

If a cognizant letter for the most recent audited indirect cost (overhead) rate is not available, the firm may submit the audit without the cognizant letter, however, the rates will be evaluated and a determination regarding their acceptance will be made on a case by case basis.

### *Applicability*

All firms requesting participation on federally funded projects are required to have an audited FAR compliant overhead rate. This requirement applies to **all engineering and design related service contracts, and professional services contracts, including sub-consultants**, entered into by the Department that are financed with Federal-aid highway funds and meet the following criteria:

- a. The contract provides for an upper limit of at least \$250,000.00 including all costs and fees.
- b. The contract upper limit is less than \$250,000.00 and:
  - i. There is insufficient knowledge of the consultant's accounting system.
  - ii. There is previous unfavorable experience regarding the reliability of the consultant's accounting system.
  - iii. The contract involves procurement of new equipment or supplies for which cost experience is lacking.

The requirements apply to all engineering related consultant agreements regardless of method of payment, including *cost plus fixed fee, lump sum, and specific rate of compensation*. Although agreements that provide for *lump sum or specific rates of compensation* will not include overhead data, this information is necessary for the Department's contracting officer to evaluate the reasonableness of the cost shown in the proposal.

## *Guidelines*

The Federal Highway Administration has approved the use of the 2010 AASHTO *Uniform Audit & Accounting Guide for Audits of Architectural and Engineering (A/E) Consulting Firms* prepared by the AASHTO Internal/External Audit Subcommittee. As stated in the Guide, “the Guide was designed to assist engineering consultants, independent CPAs, and State DOT auditors with the preparation, and/or auditing, of Statements of Direct Labor, Fringe Benefits, and General Overhead. A copy of the Guide can be obtained on the web site for the American Association of State Highway and Transportation Officials (AASHTO) under the sub-heading for the Subcommittee on Internal and External Audit: <http://audit.transportation.org> Note: The 2010 Update to the AASHTO *Uniform Audit and Accounting Guide for Architectural and Engineering (A/E) Consulting Firms* has changed substantially from the previous 2005 update. Consultants and their CPA firms should thoroughly review the 2010 updated version.

## *Requirements*

1. 23 U.S.C. Section 112(b)(2)(C) requires contracts for engineering services to be performed and audited in compliance with the cost principles contained in Part 31 of the Federal Acquisition Regulation (FAR).
2. An independent Certified Public Accountant (CPA), or cognizant government agency, must perform the audit based on **the most recently completed fiscal year**, and in accordance with *Generally Accepted Government Auditing Standards*. Consulting firms should notify their CPA that the audit should be performed in compliance with the guidelines set forth in the 2010 AASHTO *Uniform Audit and Accounting Guide for Audits of Architectural and Engineering (A/E) Consulting Firms*.
3. The audit report shall be accompanied by a schedule showing direct labor; indirect cost by account description in the consultant’s general ledger; adjustments for unallowable costs with reference to the applicable sections of **48 CFR 31, Federal Acquisition Regulations, (FAR), the Cost Principles for “For Profit Organizations”**; net allowable indirect costs; the total of these allowable costs, and the rate resulting from dividing total allowable costs by direct labor. Other data considered significant by the auditor may be included in the schedule. Examples can be found in the AASHTO *Uniform Audit & Accounting Guide for Audits of Architectural and Engineering (A/E) Consulting Firms* 2010 Edition.
4. The audit report shall be accompanied by the Contractor’s **Certification of Final Indirect Costs**. This statement, signed by an executive of the contractor/consultant, certifies that all costs included in the final indirect cost rates as presented are allowable in accordance with the cost principles of **48 CFR 31, Federal Acquisition Regulations, (FAR), the Cost Principles for “For Profit Organizations”** and do not contain any costs which are expressly unallowable under the cost principles of the **FAR of 48 CFR 31**.
5. The report shall meet the reporting guidelines provided in the applicable financial audit standards sections of the *Government Auditing Standards* as issued by the Comptroller General of the United States, and shall include **positive assurance** that all costs included in the recommended rate are allowed by **48 CFR part 31**. The auditors’ report must also include a report on internal control and compliance.

6. When annual overhead rate adjustments are required by the contract, the Arkansas Highway and Transportation Department must receive the annual certified audit report by the last day of the fifth month after the close of the fiscal year for which the report is issued.

### ***Special Considerations***

If it is in the best interest of the Arkansas Highway and Transportation Department to enter into a contract with an engineering firm that does not have an overhead rate meeting the above requirements, the contracting officer may extend a temporary waiver of the requirements and accept a provisional rate under appropriate circumstances. In order for a temporary waiver of the requirements to be granted, the Department's Internal Audit Section, under the direction of the Chief Auditor, must review the provisional rate and make a positive recommendation to the contracting officer. Also, the cost proposal must be accompanied by written assurance from an independent CPA that he/she has been engaged to audit the costs in accordance with the above requirements.

The anticipated audit must be based on costs incurred in the **most recently completed fiscal year**, with the issued audit report received by AHTD within 90 days of the provisional rate approval. If the date of the initial cost proposal is within the last quarter of the current fiscal year, the audit may be delayed until the current fiscal year is closed and the final cost data is available, provided the audit report will be issued within the specified time frame. The written assurance from the CPA that he or she has been engaged to perform the audit is still required.

Once an audited rate is approved, the upper limits provided for in the initial agreement will be adjusted with a supplemental agreement to implement the resulting increase or decrease in overhead rates, and all amounts paid the consultant prior to receipt and acceptance of an audited rate will be retroactively adjusted for changes in the rate. However, no changes in hours, fixed fees, or other costs will be allowed as a result of applying the audited rate.

### ***Field and Division Office Rates***

It is often necessary for the prospective consultant to establish a field office or use employees assigned to a division office. In either case, the consultant must submit a rate for these divisions that has been subjected to the same audit requirements as the home office corporate rate.

The 2010 update of the AASHTO *Uniform Audit & Accounting Guide for Audits of Architectural and Engineering (A/E) Consulting Firms* addresses the treatment of field office rates in chapter 5.

*\*Audit/Audited means an audit as described by the Financial Audit Standards contained in the Government Auditing Standards issued by the Comptroller General of the United States. A review, or any examination that is less in scope than an audit, will not be accepted.*

*The Arkansas Highway and Transportation Department is anticipating FHWA approval of this Executive Summary, posted to the AHTD website in April of 2011.*