

Compensation Methods for Architectural Services

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Compensation methods for architectural services take varied forms. This article discusses fees from the broadest perspective applicable to architectural services as a whole. Most architects are willing to do business under any of a number of fee arrangements; generally, the method chosen is for the convenience of the client. Definitions of the standard terms used in this article are covered in Section 2.

Section 1 - Fees

The term "fee" means the Consulting Architect's compensation for services. The method used to establish a fee should be compatible with the character of the services performed and provide adequately for salaries, office and other operating expenses, taxes, and a reasonable profit. Computation of fees for services is usually determined in one of the following ways, or a combination of the following as may be applicable for a particular project.

1.1 Lump Sum/Fixed Fee

A lump sum contract specifies that a predetermined scope of services will be furnished for a fixed fee. This amount remains fixed unless there is a change in the scope of services. A fixed lump sum fee agreement should include a stated time limit for the performance of the services. A provision should be included for additional compensation for time delays not caused by the Architect, and for changes requested by the Owner after the documents have been approved. It is essential that a detailed scope of the planned services be agreed upon under a fixed lump sum contract. Provisions should also be made for equitable adjustment in compensation should the original project be expanded or reduced in scope. In such cases, the amount of fee adjustment is often determined on a cost-plus basis.

Lump sum compensation is usually arrived at by negotiations which include the following five items:

- a. Estimated "Direct Salaries or Wages" to be paid to complete the services or the estimated "Direct Payroll Expense" to be incurred to complete the services based on the estimated number of drawings, staff hours, schedule requirements, etc.
- b. Estimated "Payroll Burden and Fringe Cost" associated with the above "Direct Salaries or Wages."
- c. Estimated "general Overhead Costs."
- d. Estimated "Reimbursable Expenses."
- e. A reasonable profit.

1.2 Cost-Plus

A cost-plus contract specifies that payments to the Architect will be determined on the basis of his or her costs for the services. This arrangement generally presupposes that the scope

of the services and therefore the costs of those services cannot be reasonably estimated at the time of contract negotiations.

For budget purposes, a contract based on a cost-plus fee may appropriately have an established upper limit beyond which the Architect is not to be compensated unless the limit is renegotiated due to a change in scope such as additional services or a change in the duration of the Project. A cost-plus fee is normally determined by one of the following two methods:

- a. "Direct Salaries or Wages" paid times a "multiplier" rate (for payroll burden and fringe cost, general overhead cost, and profit) plus "reimbursable expenses," or "Direct Payroll Expenses" times a "multiplier" rate (for overhead cost and profit) plus "reimbursable expenses."
- b. "Direct Salaries or Wages" paid plus "payroll burden and fringe cost" plus "general overhead costs" plus "reimbursable expenses" plus a fixed fee, or "Direct Payroll Expenses" plus "general overhead costs" plus "reimbursable expenses" plus a fixed fee.

These cost-plus methods are frequently used for projects for which the Architect is required to begin providing services before the total scope of services can be accurately defined, when the scope of services is complex, or when determination of the extent or duration of services difficult or impossible to determine. Such an indeterminate project generally results from the requirement for speed, special studies, research or experimental work, preparation of estimates for alternate types of construction, and other similar requirements. The project, however, should carry a general description or statement of the scope of work contemplated, such as the number, size, and character of the improvements, the extent of utilities, and other items.

1.3 Percentage Basis

Percentage basis contracts specify that payment to the Architect for a certain scope of services will be determined by multiplying a specified percentage times the awarded, estimated, or final total construction cost of the project for which the services are furnished.

"Percentage of construction cost" is a method which has been used extensively in the past for establishing compensation for professional services. Compensation based on this method is not necessarily best suited to professional encouragement and reward, since it penalizes rather than rewards the Architect for reducing construction costs through economical design. Vagaries of local construction markets may affect construction costs and create inequities in charges for professional services either to the Client or to the Architect. However, it should be recognized that the "percentage of construction cost" method has been used for many years and it may be desired by Clients who have traditionally relied on it.

Charges based on a percentage of construction cost are usually determined by one of the following methods:

- a. A mutually agreed-upon "Estimated Total Construction Cost" using unit prices established on the date of the contract for design, or unit prices expected to be current at the time of bidding.
- b. The "Final Total Construction cost," so long as care is taken in the contract to protect the Client against extremely high construction bids and the Architect against loss resulting from extremely low construction bids.

The "Estimated Total Construction Cost" is the Architect's estimate of construction cost to the Client based on plan quantities and prevailing construction costs of all elements of the

Project designed or specified by the Architect, but excluding design costs, cost of financing, right-of-way or real estate cost, legal, administrative, or other similar expenses.

"Final Total Construction Cost" constitutes the cost to the Client of actual total construction in place of all elements of the Project design or specified by the Architect, but excluding design costs, cost of financing, right-of-way or real estate costs, legal, administrative, and other similar expenses.

In Percentage Basis contracts, compensation to the Architect for such services as resident agent, property surveys, soil borings and subsurface exploration, laboratory analyses, sampling, and testing, and other "extra services" is in addition to the basic compensation.

In some instances, the Client requests preparation of alternate designs and proposals or certain portions of the project that may be deleted after design work has been performed. In such cases, the design portion of the fees should be based on the construction cost value of all alternate designs (or delete work) prepared by the Architect. For rejected alternate designs or deleted work, the compensation for design should be based on bid prices (if bids had been received) or otherwise on the Architect's estimate of construction cost. Consideration should be given to any items or changes which involve additional service or expense, but which do not reflect sufficient increase in construction cost to cover these expenses if the Architect were compensated solely on the basis of some percentage of the construction value of the change. In such cases, the changes should be provided on a cost-plus basis.

1.4 Hourly Rates for Individual Services

Hourly fees are well suited for consultation services, testimony in court, or similar work involving miscellaneous personal service. Most Architects have standard published schedules of hourly rates for various classifications of technical and non-technical employees.

Subconsultant and reimbursable direct expenses are usually billed at invoice cost plus an agreed service charge for handling.

1.5 Retainer

The employment of Architects on a retainer-fee basis is a common practice of clients who wish to be assured of always having available the services of an individual architect or architectural firm. It is also used when the services of an architect specialist are not required on a full-time basis.

The amount of the retainer varies with the character and value of the services to the Client and the reputation and standing of the consultant in his or her profession.

The terms of agreements for services on a retainer-fee basis also vary widely, and it is important that the service to be rendered be clearly defined. The compensation may be based on a fixed sum, paid monthly, or by some other mutually agreeable terms, with per diem or hourly rates for additional time spent at the request of the Client. Retainer fees are frequently on an annual basis.

The same principles as explained previously for hourly (or Cost-Plus) charges, in Section 1.2, apply to retainer-fee contracts.

1.6 Special Considerations

Projects of a special nature, such as those involving repetitive use of drawings and specifications or extensive application of standard drawings and specifications to a particular project, require special fee consideration. Charges for such services must be adequate to compensate for the estimated cost of services, the Architect's liability exposure, and to provide a fair return.

1.7 Selection of Fee Basis

The fee basis selected depends primarily on the complexity and types of architectural and engineering services to be provided. The following criteria should also be considered:

- a. Time schedule for furnishing services and possible changes that may affect the consultant's costs.
- b. Studies, programs, and other professional input furnished by the Owner or Client.
- c. Client's procedure and timing for review and approval of the Architect's recommendations/designs.
- d. Costs of administration, including records to be maintained and preserved.
- e. Probability of contingencies that are not included in the estimates of design costs.
- f. Number of third parties or agencies required to be consulted or furnished plans, specifications, reports, and similar documents.

Architectural fees are affected by many variables and it is impractical to generalize any one fee basis as preferable for a specific project.

Section 2 - Definition of standard terms and explanatory notes concerning the architect's costs

2.1 Direct Salaries or Wages

Direct Salaries or Wages are defined as the cost of salaries or wages paid to architects, planners, designers, technicians, drafters, observers, clerks, and other employees for time directly chargeable to the project. Time spent by partners or principals in the performance of technical or advisory services directly applicable to the project is to be charged as part of Direct Salaries or Wages.

2.2 Overhead or Direct Labor

Overhead on Direct Labor Costs includes contributions for social security, unemployment and other payroll taxes, workers compensation insurance, paid holidays, vacation, and sick leave, retirement benefits or pension, and medical and associated insurance.

2.3 Direct Payroll Expenses

Direct Payroll Expenses is defined as the direct salaries of the Architect's personnel engaged on the Project and the portion of the cost of their mandatory and customary contributions and benefits such as employment taxes and other statutory employee benefits, insurance, sick leave, holidays, vacations, pensions and similar contributions and benefits. Time spent by partners or principals in the performance of technical or advisory services directly applicable to the project is to be charged as part of the Direct Payroll Expense.

2.4 General and Administrative Overhead Costs

Such costs, while difficult to define due to differences in accounting procedures in various firms, do comprise a major portion of the compensation generated by the multiplier on

Direct Salaries or Wages or Direct Payroll Expense, and include, but are not limited to, the following "indirect" costs which are not directly allocable to specific projects:

- a. Provisions for office, light, heat and similar items for working space, depreciation allowances or rental for furniture, equipment, and office and drafting supplies not identifiable to the specific project.
- b. Taxes and insurance other than those included as Payroll Burden and Fringe cost, but excluding state and federal income taxes.
- c. Library and periodical expense and other means of keeping abreast of advances in technology, such as attendance at technical and professional meetings, and other professional development costs.
- d. Executive, administrative, accounting, legal, clerical salaries and expenses (other than identifiable salaries incurred as Direct Salaries or Wages and expenses, included in reimbursable expenses) plus salaries or imputed salaries of partners and principals to the extent that they perform general executive and administrative services as distinguished from technical or advisory services directly applicable to projects. These services and expenses, essential to the conduct of the business, include preliminary arrangement for new projects or assignments and interest on borrowed capital.
- e. Business promotion expenses, including salaries of principals and employees so engaged.
- f. Provision for loss of productive time of technical employees between assignments, and for time of principals and employees on public interest assignments.

Special Note: The Architect who performs services under a cost-plus contract must make provision for the accounting work necessary to segregate and record the expenditures thereof. He or she must maintain adequately detailed time records for all principals, partners, and technical employees who devote time to the project, and any part of whose salaries are included in direct cost. If contracted for, his or her applicable payroll records may be open for inspection or audit by the Client. Records of time and expenses directly allocable to the project should be provided periodically to substantiate all expenditures. The Architect should be prepared to support the basis for his or her overhead charges.

2.5 Multiplier Rates

The multiplier which is applied to Direct Salaries or Wages is a factor which compensates the Architect for payroll burden and fringe costs, for general overhead costs as previously defined, plus a reasonable margin for contingencies, and profit.

The multiplier which is applied to Direct Payroll Expenses is a factor which compensates the Architect for general overhead costs, as previously defined, plus a reasonable margin for contingencies and profit.

The size of the multiplier may vary with the type of services, the organization and experience of the Architect and geographic area in which its office is located. A higher multiplier is ordinarily necessary on projects of short duration or small size. The rate will ordinarily be higher, also, on consulting engagements for providing recommendations based primarily on experience or special knowledge, or for expert testimony in legal proceedings. It may also vary with the experience and special capabilities of the Architect.

2.6 Direct Reimbursable Expenses

Reimbursable expenses usually include, but are not limited to, the following, and are charged at cost plus a reasonable administrative charge:

- a. Transportation and subsistence expenses of employees, principals and partners

- incurred during travel in discharge of duties connected with the project.
- b. Communication expenses such as long distance telephone, telegraph, facsimile, express and messenger charges, and postage.
- c. Identifiable cost of production supplies and expenses charged to the project as distinguished from such supplies and expenses applicable to two or more projects and as distinguished from the payroll burden and fringe costs noted in Section 2.2.
- d. Reproduction costs applicable to the project, such as blueprinting, photocopying, photographs, printing, binding, etc.
- e. Subconsultant expenses for special services for associated consultants such as structural, mechanical and electrical engineering, acoustical, surveying, soil investigations, testing, observation, etc.
- f. Specialized equipment including computers, software (CADD), etc., for which a reasonable "rental rate" may be developed.

2.7 Work Done by Associate Professionals

Work performed by associated consultants, architects, and/or engineers generally falls into two categories:

- a. Work which forms a "basis for design." This work provided information which guides the Architect in his work. Little or no coordination or direction of the consultants effort is required once their scope of services is established. The cost for these types of services is customarily charged as a reimbursable consultant expense plus a reasonable administrative charge.
- b. Work performed on specialized parts of the project which is incorporated into the project design and which requires coordination and supervision during performance of the consultants services. This effort forms a part of the Architect's project design. The associate professional (usually engineers) is, in effect, a part of the Architect's staff on a part-time basis. The cost of the time for these services is customarily included as a part of the Architect's direct cost. On Cost-Plus contracts, the charge to the Client is normally based on the Direct Salaries or Wages or Direct Payroll Expense and "multiplier" of the associated consultant plus a reasonable administrative charge. On Lump Sum or Percentage contracts these costs would be included in the basic fee.

Section 3 - Payments

3.1 Time of Payments

The schedule or provisions for payment normally provide for progress payments on monthly intervals unless no significant services are provided within such an intervening period.

3.2 Payment for Additional Services

The agreement between the Client and the Architect should include provisions for payment for additional services should the project be changed, delayed, postponed or terminated prior to its completion, taking into account the following:

- a. Commitments the Architect may be required to make in anticipation of completing the project and which have been approved by the Client, including the schedule for design.
- b. Redesign requested by the Client after previously approving the design.
- c. Changes in the scope of the project.
- d. Escalation in project costs due to external influences beyond the control of the Architect affecting scope and/or time of the project.

- e. Cost and expenses incidental to termination.

3.3 Interest

The agreement between the Client and the Architect should include provisions for the payment of interest in the case of late or delinquent payment for services rendered.

Section 4 - Records

Any Architect performing services under an hourly or cost-plus type contract is obligated to segregate and record the expenditures thereof and to maintain adequately detailed records. These records should be open for inspection by the Client.