AIA Best Practices:
Setting fees: What to consider

Contributed by David B. Richards, FAIA, LEED AP, PMP. Excerpted and adapted from The Architect's Handbook of Professional Practice, 15th edition.

Summary

Based on the scope of the service, an architect needs to understand the effort required, the associated risks, and the value of the services provided to set fees. In addition, begin with the end in mind and use contingencies to be able to adjust to project conditions and to ensure that the project makes an appropriate profit.

Understand the scope of service

When setting fees, it is essential to understand the scope of services to be provided. Most often basic services are required, and based on input from the client additional services may be desired or needed. Work to establish a common understanding of the scope of service with the client, and help the client understand the services they will receive.

Some clients, such as those who frequently purchase services from architects, will be able to define the specific services required for their project; others will need to learn about the process an architect uses to design, document, and administer their project. Architects experienced in a project type will also know the effort required to provide the required service.

- Review the scope of services with the client; understand their special needs and specific desires for the project.
- Will the client need to review multiple design iterations?
- Do they need full time representation during construction?
- Define any special or additional services in the agreement for professional services.
- Review the scope of services in the agreement with the client to foster a mutual understanding.

Analyze the effort

Based on an in-depth understanding of the scope of work needed for the project, the specific needs of the client, and the risks in the project, analyze the scope of work in a work breakdown structure (WBS). The WBS divides the project into phases. Each phase is further broken down into the individual tasks required to complete the phase. Each task is budgeted with hours and/or dollars, and the totals are accumulated in a

total net fee. Provide a contingency of hours to allow for variations from the plan. Build up the fee based on all of the tasks and activities that will be required to deliver the completed project.

Review the risks

Starting in the late 1970s, professional liability insurance industry providers encouraged professionals to avoid any risk in delivering services. But, as professionals, we as architects have responsibilities that are associated with risk. The key is to identify and understand the risks that are beyond what is normal, such as unknown or unpredictable project conditions.

Resolution of risks may mean additional effort by the architect or additional consultants added to the team. By analyzing the potential risk, the architect can include the hours/dollars in the fee to resolve the risk or pay the consultant. Fees for project-specific risks may be offered as an if-needed additional service but should be defined at the onset of the project.

Understand the value

An architect's services are more valuable than the cost of delivering the service. The value of services can be related to special talents, unique abilities, speed of delivery, specific project knowledge, or exceptional design ability. Unique specialized services or abilities are valuable to clients, and architects that offer these should structure fees to benefit from those unique abilities and services.

An architect should work to understand the marketplace to know the value of their professional services. Specialized knowledge of a building type may result in the services being worth 20 to 30 percent more than the cost of providing those services. The ability to deliver a project faster than the competition can be especially valuable to the client. It can save them project costs in many ways and may increase the value of services 10 to 20 percent. Other unique consulting abilities offer similar value to the client—value that is reflected in higher fees.

Build fees in three ways

After the effort, risk, and value have been considered, it is a good practice to build a fee three different ways. One is to build the fee bottom-up based on effort. Another is a top down fee analysis based on comparable past projects or rule of thumb gross fee determinate. And a third is a duration-based analysis that considers that the effort will take x number of staff y weeks to complete the project or phase. Building a fee bottom-up, top-down, and a side view provides a check comparison. When the three methods begin to result in the same fee, then the fee is likely appropriate for the project.

Bottom-Up Analysis

The bottom-up analysis considers the effort associated with each task in each phase of the project, and it includes the effort to resolve risks. Fees determined from a bottom-up analysis tend to be higher than other methods because all effort and risk is considered. If the situation is well understood and everything that can go wrong is taken into consideration, this fee will tend to be too high and non-competitive. The bottom-up analysis should be balanced with the top-down analysis.

Top-Down Analysis

A top-down analysis takes a different perspective on the project. This approach is based on having an idea of what the total fee should be at the beginning. In a top-down approach, determine the appropriate fee for the project based on experience with the project type/past projects, the specific market, and the competition, and consider the fee based on a percentage of construction cost or other unit cost approach. The result of this effort is to determine the gross fee for the project.

Once the total fee has been determined, distribute that fee among the consultants, allow for contingencies, and then determine the total net fee available for the architectural work. Divide that fee among the phases, determine the total hours available for each phase, and apply hours to the task list; work backward from the gross fee into the hours available for the phases and tasks of the project.

A top-down analysis might verify a bottom-up analysis, or it might indicate a need to reconsider both approaches to find a common solution. Often the bottom-up analysis will result in a higher fee than a top-down analysis. Working the fee from two approaches and challenging the results of both approaches can help work the fee into the right place.

It is good practice to keep track of fees for different project types along with actual project performance. Metrics such as the fee as a percentage of construction cost, cost per square foot, hours per square foot, hours per construction cost, and project multiplier all provide historical input for comparison when setting a fee.

Staff Analysis

Another way to determine a fee is to consider the durations and staffing required for completing a phase. One might consider that it will take two staff members four weeks to complete the schematic design phase. This can be used as another comparison to the bottom-up analysis of the effort and the top-down fee comparison.

Working back and forth among these fee approaches will work the fee into the right place. When the fees from all three analyses are very similar, then the fee is likely about right. It is important to consider value when determining the fee.

Consider the value of the services to the client: Does the firm compete to provide commodity type services that are readily available from many firms in the marketplace, or are services offered that are unique to the market? Does the firm have a special edge in design? Program management? Unique project experience? Is there any reason that a client would pay in excess of the effort required to provide services? If the answer is yes, then increase the fee accordingly.

Contingencies

Include contingencies in the fee planning to allow for unforeseen events. Consider three types:

- **A contingency that there is no intention to spend.** This may be a way to define the initial 10 percent profit in a project plan.
- **A contingency that there is intention to spend.** As the work effort is defined in terms of hours per phase per discipline, build a contingency of hours into the plan. These hours will be used to adjust the plan to actual, and to respond to variations in the delivery of the project. Ten percent of hours is a good starting point for this contingency. That allows for 2 to 4 percent variances in the planned hours in each phase.
- **A contingency that is there for special situations**— one that there is not an intention to spend but is there in case additional effort is required. This contingency might be about 3% of the fee.

About the contributor

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Architect's Handbook of Professional Practice, 15th edition Unit 1 - The Profession
Chapter 15 – Project Definition
Section 02 – Services and Compensation