October 2022

Considering Overhead and Profit in IPD

A Position Paper

INTEGRATED PROJECT DELIVERY ALLIANCE

Table of Contents

Acknowledgements

This paper is the work product of the “Contract and Numbers Working Group,” an ad hoc committee of IPDA members from across the industry and has been reviewed and approved by the IPDA Board of Directors.

IPDA Contract + Numbers Working Group
Markku Allison, Chair | Chandos Construction
Bill Lett | Lett Architects
Dean Loewen | Altac Mechanical
Deon Wilner | ISL Engineering
Geza Banfai | McMillan LLP
John Ford | LEA Consulting
Nick Berci | Entuitive
Rick Pews | City of Barrie
Brad Stevenson | Unitech
Craig Webber | Group2 Architecture
Ken Jaeger | KTJ Consulting
Louise Panneton | P1 Consulting
Maria Williams | Chandos Construction
Glenna Armitage | Group2 Architecture

IPDA Board of Directors 2022
Lynnell Crone, IPDA President | Bird Construction
Bill Lett | Lett Architects
Craig Webber | Group2 Architecture
Markku Allison | Chandos Construction
Daniel Drouin | Group2 Architecture
Dean Loewen | Altac Mechanical
Jen Hancock | Chandos Construction
John Ford | LEA Consulting
Kelly Fawcett | P1 Consulting
Ken Jaeger | KTJ Consulting
Patrick Taylor | WSP
Rick Pews | City of Barrie
Stephani Carter | EcoAmmo

Introduction

A continual area of challenge for companies and teams entering into IPD projects is understanding exactly how overhead and profit are handled. On what are they based? How are they calculated? What's included or excluded? Designers and constructors calculate them differently--why is that, and how are those differences accommodated? These are just a sampling of the kinds of questions that typically arise.

The purpose of this position paper is to suggest answers to these and other related questions as well as common definitions for relevant terms. Based largely on the CCDC 30 - 2018 and the Hanson Bridgett 2019 IPD Agreements and written by experienced IPD professionals and shared publicly, the goal of this paper is to improve transparency and provide clarity to the market and the RFP process, helping owners, individuals, companies, and teams navigate the topic by suggesting specific solution paths (and outlining their ramifications), showing examples, and providing sample calculation templates.

This paper is the work product of the "Contract and Numbers Working Group," an ad hoc committee of IPDA members from across the industry and has been reviewed and approved by the IPDA Board of Directors. As such, it represents the official stance of the IPDA on matters contained herein as of its publication in early 2022.

Why do we need this paper?

There are a number of IPD contracts in common use in the North American industry market today, including but not limited to Canada's CCDC 30, the AIA's C191 family, ConsensusDocs 300 series, the Hansen Bridgett agreement, and a range of custom agreements. These contracts generally have similar moving parts, but the differences in specifics can be important, especially in areas like the definition of overhead, profit, direct cost, etc., and how they fit into financial calculations.

Our goal is to focus on the financial calculations elements to create an objective resource for the market. Industry stakeholders would be well served to get this paper in the hands of owners prior to issuing RFPs; while it is not our intent to give advice on creation of an entire RFP, the recommendations we give here (if followed) will enhance clarity and consistency for owners issuing RFPs and for architects, GCs, consultants, and trade contractors in responding to RFPs. By creating a consistent approach to calculations of OH+P we can increase the ability of respondents to truly submit comprehensive apples-to-apples numbers, allowing teams and owners to have greater confidence when reviewing submissions. Specifically, the numbers we'll be looking at, defining, and making recommendations about include:

1) Overhead
2) Labour rate
3) Payroll burden
4) Material costs
5) Profit expectation

The set of recommendations in this paper are aligned with the spirit of IPD. They are rooted in fairness, trust, and respect, and recognize the goal is not to gouge nor to squeeze and that everyone is entitled to fair profit and costs. IPD is also all about transparency, which allows elimination of financial waste through redundancy and/or double dipping both through the open-book nature of the model as well as the fact that numbers are auditable.

This paper is targeted primarily at Canada's CCDC 30 contract, though the concepts can easily be adapted for other IPD contracts. The recommendations being made will likely require inclusion in the supplemental general conditions of the CCDC 30, though it is our hope that the contract will evolve to adopt these as standard language. Please note also that while this paper is crafted by industry professionals experienced in IPD, based on their personal experience and best practices they've encountered, you may wish to seek the advice of your legal counsel, and that owners are advised to seek input of their procurement teams to ensure compliance with the requirements unique to their organization.

Observations and Considerations

Before we move into recommendations regarding basis for calculations, it will be helpful to look at industry context. How different stakeholders have traditionally approached these things can have a strong impact on moving to new models of thinking (and calculating).

Consultants and constructors have long existed on two sides of a wall. Historically, they have different mindsets and cultures. Generally speaking, consultants have seen themselves as owner advocates. As big picture thinkers, always modeling divergent to convergent design thinking, consultants have felt only loosely responsible for costs, generally conscious of but wanting constructors to lead actual cost discussion. On the other hand, constructors have generally been very practical as well as cost and schedule conscious, problem-to-solution oriented, focused on execution.

Differences between the two stakeholder groups continue when we look at how they've historically made their money and charged for their work. Consultants (professionals) charge for time (labour-based), usually through some structure of hourly rates, percentage of project costs, or a fixed fee. They generally include a markup on sub consultants to cover risk, tax burden, and coordination time. Conversely, constructors charge for both labour and materials, recovering job-related costs through general conditions, markups on materials, sub trades, equipment rental, and on some projects, on consultants and subconsultants as well. Typical models for payment include fixed fee / lump sum, time and materials, and cost plus. Both groups charge for reimbursable expenses, though what's categorized as "reimbursable expense" can vary greatly between the two.

It's also important to recognize other dimensions of difference, such as small vs large or public vs private. Considering size of organization, there can be significant differences in profit and overhead figures, in the ability to allocate resources, obtain certain types or levels of insurance, as well as geographic reach or jurisdiction of operations. Small organizations may be more agile, but with a greater depth of resources at times larger organizations may be more responsive. Public entities may have a different responsibility to shareholders or stakeholders than private entities, as well as different insurance requirements and ability to respond based on staffing. And different cultures are almost certain to arise as a result of these differences.

As we start to consider IPD, we will find that things are different, and that new perspectives are required--old perspectives belong to current or past context, and may not be helpful for IPD. Regardless of origin, it is critical to have a consistent understanding on which to build an appropriate basis of calculations for IPD.

Basis for Calculations

Different IPD contracts address the basis for overhead and profit calculations differently. Different models are also emerging, with some teams opting to base everything solely on the scope of the individual party, and other teams looking to enact models where the GC's basis for calculations during validation and design differs than the basis during later phases of the project.

Many of these variants are most effective with experienced IPD owners and teams and can be confusing and even risky with owners and teams new to IPD. IPDA's goal with this paper is to outline and recommend the most common practices we see in the market today as a baseline approach for maximizing clarity and consistency. Given that goal, IPDA recommends the following as the basis for overhead and profit calculations on IPD projects.

a) Costs
   i) Payroll Burden
      1. See following matrix for IPDA recommendations.

Payroll Burden Specifics	Included in Payroll Burden	Excluded from Payroll Burden	Direct Chargeable Cost
Canada Pension Plan (CPP)	x		
Employment Insurance (EI)	x		
Workers Compensation	x		
Employer Health Tax	x		
Health Benefits	x		
RRSP or Pension Contributions	x		
Vacation	x		
Statutory Holidays	x		
Vehicle Allowance: Taxable benefit vehicle allowance	x		
Absent Days of anykind as supported by company policy in effect as of the contract signing (Earned days off, bereavement, sick days, etc.)	x		
Pre-existing contractually defined salary premiums (non-discretionary) not connected to profit	x		
Bonuses or profit sharing of any kind not included in the above (retention, spot, holiday, referral, signing, etc.) are not eligible		x	

   ii) Overhead
   IPDA recommended basis for OH:
      1. Prime Consultant: based on your scope of work.
      2. Other signatory Consultants: based on your scope of work.
      3. Other non-signatory Consultants are direct flow-through to poly-party.
      4. GCs: based on your work plus managed construction-side stakeholders, trade partners, and lump-sum trades ("cost of the work")

   a. Whether IPD partners or not, whether they perform the services or not
   b. More likely to be industry standard
   c. Inclusion of design-side costs is discouraged in the basis of calculation for the General Contractor.
5. Other trade partners: based on your scope of work.
6. Items to be considered as overhead
   a. See following matrix for IPDA recommendations.
      Note: highlighted lines are often subject to discussion and negotiation.

Overhead Specifics	**Included in Overhead**	**Excluded from Overhead**	**Direct Chargeable Cost**
The DSE + PBR associated with General Office Adminstration Staff	x		
Shared Office Staff: Estimators, pre-construction, etc.			x
Advertising, Marketing & Promotion Costs	x		
Automotive: costs directly associated with company vehicles not on project (not equipment)	x		
Automotive: mileage charges (for personal vehicles w/o vehicle allowance)			x
Bad Debts		x	
Bonuses or profit sharing of any kind not included in the above (retention, spot, holiday, referral, signing, etc.)		x	
Building Repairs & Maintenance	x		
Business licensing	x		
Communication Network: telephones, internet, or mobile devices	x		
Customarily Worker Owner Tools, Company Tools & Materials	x		
Depreciation of Assets	x		
Donations		x	
Health & Safety (PPE)	x		
Income taxes		x	
Insurance	x		
Interest on long-term or callable debt (ALL including firm acquisition, major asset financing, etc.)		x	
Interest and bank fees	x		
Office Supplies	x		
Reproductions (day to day business operations)	x		
Reproductions (project specific)			x
Professional Dues & Memberships	x		
Professional Fees associated with General Office Administration only (ie. Accounting)	x		
Rent	x		
Tools under $500	x		
Tools over $500 (a discussion of salvage value and post-project ownership is important)			x
Training & Continuing Education	x		
Travel (a discussion about limits and distances of travel is important)			x
Meals & Alcohol / Entertainment (discussion of restrictions of public and other owners is important)			x
Utilities	x		

b) Profit

IPDA recommended basis for profit:

1. Prime Consultant: based on your scope of work.
2. Other Signatory Consultants: based on your scope of work.
3. GCs: based on your work plus managed construction-side stakeholders, trade partners, and lump-sum trades ("cost of the work")
    a. Whether IPD partners or not, whether they perform the services or not
    b. More likely to be industry standard
    c. Inclusion of design-side costs is discouraged in the basis of calculation for the General Contractor.
4. Other trade partners: based on your scope of work.

c) Rationale

IPDA's rationale for basis of calculations is principle based:

1. Alignment with current industry practices and cost recovery models will produce the most accurate costs and doesn't require alternative accounting protocols to support a contract model within the industry.
2. Removes all barriers for scope adjustments, scope swaps, or workflow adjustments from the GC and the Prime Consultant.
3. Overhead recovery is consistent with industry standards for trades based on labour and materials. If modified to be based on labour only the method of calculation could disincentivize potential productivity gains.

Key Principles

A short list of general principles to consider in matters regarding overhead and profit.

1) Profit and overhead are NOT bad things.

2) Remove all profit from overhead.

3) Remove directly charged items from overhead.

4) You are not eligible to recover costs not recovered on conventional non-IPD projects.

5) Unless agreed otherwise, if the project pays for something it belongs to the Owner at the end of the project.

6) Discretionary categories within business operations should be excluded for OH calculation and included in Profit calculation:
    a) Dividend payments
    b) Donations
    c) Bad debts
    d) Long term acquisition financing or financing on equipment (where cost of financing is built into the amount charged and recovered through use).
    e) Labour and costs associated with the creation of a capitalizable asset (IT costs associated with software development, etc.)
    f) Costs associated with separate business units (mining vs. construction)
    g) Costs associated with non-Canadian operations (corporation with global head office in Canada costs would be allocated across global operations not found only in Canadian operations)

Things to watch for in RFPs, contracts, and practice

A short list of things to watch for and consider in the areas of overhead and profit on IPD projects based on direct industry stakeholder experience includes but is not limited to the following:

1) Lack of clarity and consistency
    a) Even with a well-defined and consistent approach to calculating OH+P on IPD projects, owners need to be diligent and watch for errors and inconsistencies. Because IPD is still relatively new, and the basis for calculations for OH+P (as well as the stakeholder relationship to profit) are different, it is not uncommon to see errors in submissions. If there are significant differences in figures submitted by proponents, it's likely that one or more have used a different method for calculating. If not flagged and followed up, it can result in inappropriate contract awards. This is sometimes manifested in big differences in OH that are hard to track down. It may also be that a proponent or organization is not just covering costs but making undue profit, or, conversely, losing money due to them under the IPD model.
    b) Owners should provide clear instruction for adding OH to base rates as well as itemized lists and basis for calculations of what is in OH vs reimbursable or in profit during procurement processes / in the RFP.

2) Confidentiality of data
    a) It is important to be mindful of who has access to what, as well as the sharing of that information. Areas to watch for in particular include but are not limited to the contract itself, rate sheets, and invoicing.
    b) It can be helpful to consider using position titles and "banding" instead of naming specific individuals and their salaries. This is supportive of confidentiality, but has implications for how we ask for information as well as an impact on auditing.

3) Terminology and restrictions around hourly compensation
    a) Can't charge more for salaried staff than they cost.
    b) Overtime variances and approvals (should again be based upon actuals). It can vary from hours per week or hours per day in different provincial jurisdictions.

4) Unless otherwise captured in the IPD agreement, personal equipment or transportation allowance(s) will be either a taxable benefit and be included in Direct Personnel Expense or a company expense and included in the overhead, depending on how the IPD team member accounts for it within their company and by individual (tax records would be auditable).

5) Identify procedures for modifying and escalating rates. For instance, typically it is a once yearly allowable escalation as opposed to individual basis change. IPDA suggests raises

(hence rates) should be a standing item on a PMT meeting once a month.

6) Try to guard against double-dipping. For example, taxable benefits being included in overhead calculations or reimbursable costs.

7) Material or physical items that are not a rental item but will be consumed, incorporated, or delivered to the Owner after the project is complete are Direct Costs.

8) IPDA recommends the development of a table of approved rental equipment.

9) In cases where a threshold of cost for post-project ownership of tools by the design and construction team is identified, IPDA recommends that threshold be set at $500.

10) Owners and teams should think critically about allocation of safety and safety personnel costs between overhead and cost of the work.

11) In cases where the Owner directs all project billings (including design) to flow through the GC there may be reason to consider accounting costs that may otherwise be allotted as overhead, to be chargeable as direct recoverable costs.

12) Interest on profit: Payment of interest on profit should be considered if requiring Lien holdback from contractor and consultants. The cost of money to carry this is a new requirement of the IPD contract and would not be found within the basis of overhead calculation for any of the companies, therefore it should be considered as a separate element in developing overhead for the project or covered in the contractual terms issued by the owner. IPDA posits that it would be more transparently dealt with in the industry if it was covered within the contractual terms of the contract as it could be clearly adjusted based upon achieving milestones

Conclusion

IPD is still relatively new and is evolving. Consistency, clarity, and transparency around financial matters in IPD is critical, especially during the selection process. It is IPDA’s hope that this position paper will help owners and industry bring greater consistency and transparency to the IPD process.