4

Fees and expenses

Some basics

There is no magic formula for determining the level of fees that will provide 'value for money'. Hence the need for competitive bidding as an indicator of 'market price'.

Large, established firms are likely to charge more. But the trade-off is that they may be able to respond better to any problems that arise during the project, so that overall risk to the government agency is reduced (although they may charge extra for solutions). This may not be apparent from the bid (submission) itself, but should be taken into account in gauging value for money.

On the other hand, small consulting firms may be more responsive to client needs than large ones. They are less likely to try to sell a pre-packaged approach or solution. Assuming the same level of skill as larger firms, they may therefore provide better value for money. However, they may represent a greater risk in terms of availability of personnel and ability to meet unforeseen needs and problems.

Fees can provide a lever for influencing a consultant's performance. A graduated, incentive-based scale that reflects differing degrees of performance is better than an 'all or nothing' penalty approach.

Payment schedules should be based on carefully defined and specific milestones. Of particular importance is that the milestones are easily measurable. Smaller firms may need more frequent milestones to ensure adequate cash flow for their continued operation.

If consultants are not registered for GST, then the entity that hires them will not be able to claim an input tax credit for the fee paid. To maximise cash-flow benefits to the entity, the contract should specify that tax invoices will be required for any payment to the consultant, unless they prefer not to obtain an Australian Business Number (ABN).

In some cases, it may be difficult to specify clearly the extent or quality of work required. Providing a ballpark figure (maximum, or a range) for the value of a job in tender documentation can 'signal' bidders to compete primarily on quality, with less emphasis on cost. Value for money is encouraged because excessively expensive bids, as well as superficial proposals, are avoided without eliminating price competition entirely.

Travel and accommodation expenses are usually charged at cost at non-Senior Executive Service (SES) rates. Consultants do not normally receive a travelling allowance, so the contract should specify that expenses are to be acquitted on the basis of receipts. A further possibility is to place a contractual cap on total expenses, in order to minimise costs.

Various payment arrangements are possible. Shenson (1990, Chapter 9) identifies a number, including the following:

- *Daily or hourly fee*: there is little incentive for the consultant to minimise the time spent on the job and the client bears all the risk.
- *Fixed-price fee*: the consultant bears the risk and is likely to have allowed a contingency margin in the bid, although it is unlikely to be apparent to the client. In an arrangement of this kind, it is important to have well-defined outputs.
- *Fixed fee plus expenses*: the most common form of contract used in the Australian Public Service. While the consultant bears the risk for the fixed fee, the client bears the risk of expenses unless the contract specifies that expenditure for expenses is subject to prior approval.

- *Fixed-price plus incentive*: if a special condition is met (for example, early delivery) an additional pre-specified fee may be paid to the consultant. An alternative form is to base the fee on an estimate by the consultant, for example $50,000, with a capped fixed price of $70,000. It can be agreed that any costs above the $50,000 threshold (but not exceeding $20,000) will be borne by the client at a rate such as 75 per cent, and the remainder by the consultant. This approach provides an incentive to the consultant to minimise costs above $50,000, but without necessarily compromising the quality or extent of the contract outputs.
- *Graduated incentive fee*: if the consultant estimates that the contract will require $50,000 of work, a range of $20,000 can be set on either side. The consultant may be required, for example, to bear 25 per cent of costs above $50,000 up to a maximum of $70,000. Similarly, the consultant may receive 50 per cent of any savings below the estimated project cost of $50,000.
- *Fixed-price with re-determination*: Where the scope and nature of the work is very vague, the parties may agree to proceed for a fixed fee to a defined milestone, by when the requirements will have been better defined and a fixed fee for the remainder of the work can be agreed.
- *Cost contract*: where the consultant will acquire technology or knowledge which can be used to earn profits elsewhere, it may be possible for the client to agree to pay some portion of the consultant's costs, but no fee (to reflect the revenue potential of the technology). This approach may be suitable for dealing with intellectual property.

Australian Government requirements

Apart from the broad provisions of the *Public Governance, Performance and Accountability Act 2013* regarding the 'proper use' of Commonwealth resources (see Chapter 2), obtaining 'value for money' is the primary guidance provided to government agencies of relevance to consulting services.

Contract fees may be affected by the extent of liability accepted by, or imposed on, the contractor. In general, liability should generally rest with the party best placed to minimise the occurrence of an identified risk, and any limitation of a contractor's liability should be based on comprehensive risk management.

Tips and traps

- Public servants are sometimes not aware of the fact that consultants normally consider time spent in **meetings with the client** to be **billable**. If the contract specifies that a certain number of consulting days (usually taken as 7.5 hours per day) will be spent on the project, then any anticipated meeting time should be taken into account in setting the budget for the project. Top-tier firms will not normally bill for time spent travelling to a meeting unless **travel** occurs during business hours and precludes the consultant from undertaking other work, but air and taxi fares and accommodation are considered to be legitimate expenses to be reimbursed by the client. (Consultants are generally reimbursed at non-SES rates. Unlike some public servants, they do not normally receive a daily travelling allowance.) Items such as **faxes** sent to clients, **telephone calls**, use of **couriers** and other out-of-pocket expenses are also considered to be expenses that are recoverable from the client. And don't forget to allow for time spent on project **management** tasks or the use of **materials** (printing multiple copies of reports can be expensive). Because practice differs widely between consultants, it is worth checking on each bidder's charging policy for all of these 'pass-through cost' items. Bidders are likely to be more accommodating if you do so in the request documentation.
- Whether you should **expect to pay a fee** each time that you deal with a consultant depends to a large extent on your relationship. There are no hard and fast rules, but the following provides some general guidance:
  - If you want to test the feasibility of a project and phone a consultant to 'pick their brains' in a general way, they will normally treat the enquiry as part of their marketing activity. But the consultant is likely to follow up in a few days to see if you want some work done. So be careful not to raise undue expectations during the first query.

- Frequent calls for (free) opinions to a tax consultant, on the other hand, would probably come to be seen as unwelcome if no paid work flowed from the queries.
- Asking a consultant for a 'one-page outline' on how to deal with an issue is likely to be seen in the context of a proposal. A 'proposal' comes closer to generating an expectation that work is available. It is worth making clear that you are still only in the stage of considering the possibilities. Except in very large projects, proposals may be provided free, although consultants themselves will consider whether it is worth their while preparing them for a specific enquirer. Unless you offer definite work, however, do not expect a full analysis that solves your problem.
- Once you ask a consultant to put together a proper plan (even a few pages), you start to cross the line into making serious use of a consultant's expertise and time and a fee should be expected. Caution is therefore required to avoid entering into an implicit contract, without considering fully the need for a consultant and the need for a tender process.

• Some agencies appear to select consultants purely on the basis of quoted cost, apparently avoiding larger firms. Unless all factors, including quality of output, are taken into account, the chance of obtaining **value for money, the primary consideration**, will be diminished.

• Where project outcomes are not entirely certain, or there is some likelihood that the analysis may point to further work, consider allowing for a **contingency amount** of, say, 10 to 15 per cent of the total project budget as part of the estimate of expected value of the procurement under CPR clause 9.2. Note that CPR clause 9.6 states that 'when the maximum value of a procurement over its entire duration cannot be estimated the procurement **must** be treated as being valued above the relevant procurement threshold'.

• Most consultants try to remain **competitive**. If consultants refuse to lower their fee in a competitive situation, their **quote** is likely to be fairly realistic for the proposed level of quality and time spent. If you are still not happy with it, ask an experienced colleague for advice, or even ask another firm (but be careful about commercial confidentiality). Alternatively, explore the possibility of reducing the scope of the work if budgetary considerations are of concern.

A refusal to accept a lower fee may be an indication of a good consultant who is in demand and can earn that fee elsewhere. And if a consultant does accept a fee that is lower than they wish, they may later cut corners to ensure they do not make a loss.

- Government entities sometimes seek to reduce risk to themselves by specifying a **fixed-price contract**. However, establishing the price in a reasonably competitive market means that the consultant is likely to insist on keeping strictly to the scope of the work defined in the contract, because there is little margin to adjust without incurring a loss. A client may therefore gain more certainty regarding the final amount to be paid to the consultant, but may bear a commensurately higher risk in terms of output if changes to the scope of the work are found to be required during the project. Because most projects require some adjustment as they proceed, neither side is likely to end up being entirely happy with the final outcome. Potential problems can be reduced, however, by ensuring clarity of requirement in the request documentation. Alternatively, provide in the contract for the ability to agree easily on changes to work specified. Such potential changes should be expressed in the form of options to ensure that they form part of the initial contract.

A major area of frustration to consultants is the **unavailability of data or personnel promised by clients**. The assumption that data are available is likely to be a significant factor in the framing of a bid: collection of original data is usually expensive. If there is any uncertainty about the quality or availability of data, bidders should be invited to inspect it for themselves as part of the tendering process, rather than specifying in request (tender) documentation that data will be made available. Similarly, if bidders were promised a contribution of personnel to help with the project, you need to make sure that they are available at the times when they are needed. If you do not make available data, staff, or other resources promised during the tender process, you should expect to meet any expenses incurred by the consultant in making up the shortfall. Delays are also likely.

Table 4. Fees and expenses: Risks and mitigation

Type of risk	Likely consequence	Mitigation strategy
Fee is too low	Consultant loses incentive to produce quality or timely output Possible request for renegotiation during contract	Fair negotiation of fees, possibly 'fixed price plus incentives' version Include options for additional work in contract Periodic review during contract Build a contingency allowance into the budget for the contract
Insufficient provision for expenses	Budget overrun for entity Lower quality output; reduced value for money	Request estimate of expenses over life of project as part of the submission Specify that only written variations to contract can result in extra expense Periodic review during contract Build a contingency allowance into entity's budget for the contract Contract should specify expense reimbursement only on basis of receipts Cap on expenses in contract
Fees or expenses too high	Reduced value for money	Encourage competitive bidding Develop strong working relationship with consultant from the outset to encourage fair dealing (and possible refund) Request cost breakdown with all invoices (including record of hours worked)

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