

**INNOVATIVE STRATEGIES FOR
CONTRACTOR COMPENSATION**

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COMPENSATION STRATEGY GROUPING

Compensation strategy	Example benefit of strategy
A. DEVELOPMENT OF INCENTIVE PLANS	
1. Fee-at-risk proposals solicited from contractors during bidding	\$3.3 million savings on \$120 million project, schedule reduced from 36 to 30 months (CS4)
2. Incentives developed during project kickoff and teambuilding sessions	27% cost underrun relative to budget, 1.5 month reduction in 8 month schedule (CS6)
3. Incentive plans introduced during project execution	20% cost underrun, 2 month early completion (CS2)
4. Standard framework for incentive plan development	All production yield targets exceeded with plant performance incentive plan (CS6)
B. SELECTION OF PERFORMANCE MEASURES	
1. Benchmarking to set performance targets	2.4 % improvement to owner return on investment for project (CS14)
2. Incentives on joint performance of designer and constructor	3 month early completion on 24 month project (CS6)
3. Subjectively determined fee at owner sole discretion	2 month early project completion (CS8)
4. Incentives on plant performance	4% improvement in plant production availability (CS3)
5. Non-traditional incentive areas	Reduction in defensive documentation on project, commitment to owner goals (CS4)

Figure 4. Innovative Contractor Compensation Strategies

COMPENSATION STRATEGY GROUPING

Compensation strategy

Example benefit of strategy

E. INCENTIVE EFFECT IMPROVEMENT THROUGH INCREASED CONTRACTOR CONTROL

1. Small, empowered owner team
Successful execution of \$115 million project with staff of two owner personnel (CS5)
2. Co-project directors, for owner team
A "new project delivery" method for owner (CS4)
3. Extensive preliminary engineering
Owner ability to negotiate contract with contractor profit and overhead at risk (CS1)

F. MAINTENANCE OF INCENTIVE CONTRACTS IN LONG-TERM RELATIONSHIPS

1. Continuous improvement of performance targets
Steadily improving contractor performance over four-year period (CS3)
2. Competition between alliance partners
All work performed within budget (CS3)
3. Periodic bidding of work to contractors outside of alliance
Alliance contractor overhead charges reduced 22% (CS3)

G. PROMOTING LONG-TERM CONTRACTOR FOCUS ON OWNER OBJECTIVES

1. Incentive on production output
Contractor focus of production issues (CS12)
2. Contractor assumption of equity risk
Best contractor resources allocated to owner's project (CS11)

H. FUTURE WORK AS A MOTIVATOR

1. Opportunity to bid future work packages as an incentive
Construction contracts awarded and completed below budget (CS3)

Figure 4. Innovative Contractor Compensation Strategies (continued)

COMPENSATION STRATEGY GROUPING Compensation strategy	<i>Example benefit of strategy</i>
I. ALTERNATIVE COMPENSTION UNITS	
1. Inclusive hourly rate for engineering services	<i>Simplicity of invoice approval and demonstration of innovativeness (CSB)</i>
2. Inclusive engineering multiplier	<i>Simplified invoice approval, reduced owner administrative staff (CS10)</i>
J. CASH FLOW ENHANCEMENTS	
1. Shorter payment terms	<i>Access to cost competitive local contractors (CS5)</i>
2. Partial up-front payment of fee	<i>Immediate attention of contractor upper management, increased vendor response (CS10)</i>

Figure 4. Innovative Contractor Compensation Strategies (continued)

WHY USE INCENTIVES?

MUST CONTINUOUSLY IMPROVE THE WAY WE EXECUTE PROJECTS TO REMAIN COMPETITIVE:

- **CREATE INCENTIVE FOR CONTRACTORS TO FOCUS ON BUSINESS OBJECTIVES**
- **ALIGN PROJECT TEAM MEMBERS' GOALS WITH BUSINESS OBJECTIVES**
- **CREATE INCENTIVE FOR PROJECT TEAMS TO EXCEED BUSINESS OBJECTIVES**

Examples of Milestones/Criteria

Business Value	Examples of Performance Milestones/Criteria
Quality	<ul style="list-style-type: none"> • Rework (design/construction) • Customer satisfaction • Noncapital cost for design reviews, change orders (C/Os), start-up (S/U) • Facility performance six months after start-up • Completeness of design packages • Change orders
Cost	<ul style="list-style-type: none"> • Total project cost vs. estimate • Productivity factors (design/construction) • Growth of lump-sum packages • Engineering and home offices (E&HO) costs • Construction management costs • Cost-saving ideas
Schedule	<ul style="list-style-type: none"> • Material management • Mechanical completion (M/C) • Interim turnover (T/O) • Design package issues • Product commercialization • Shutdown (S/D) duration
Commercial Start-up	<ul style="list-style-type: none"> • Speed with which commercial product produced. • Start-up cost versus expectations • Quality of product produced.
Facilities Operation	<ul style="list-style-type: none"> • Reliability of plant or specific equipment • Cost of goods • Maintenance cost versus expectations
Technology	<ul style="list-style-type: none"> • Innovative technology