CONTRACT PRICING TYPES

PRICING TYPES

FEED Contracts

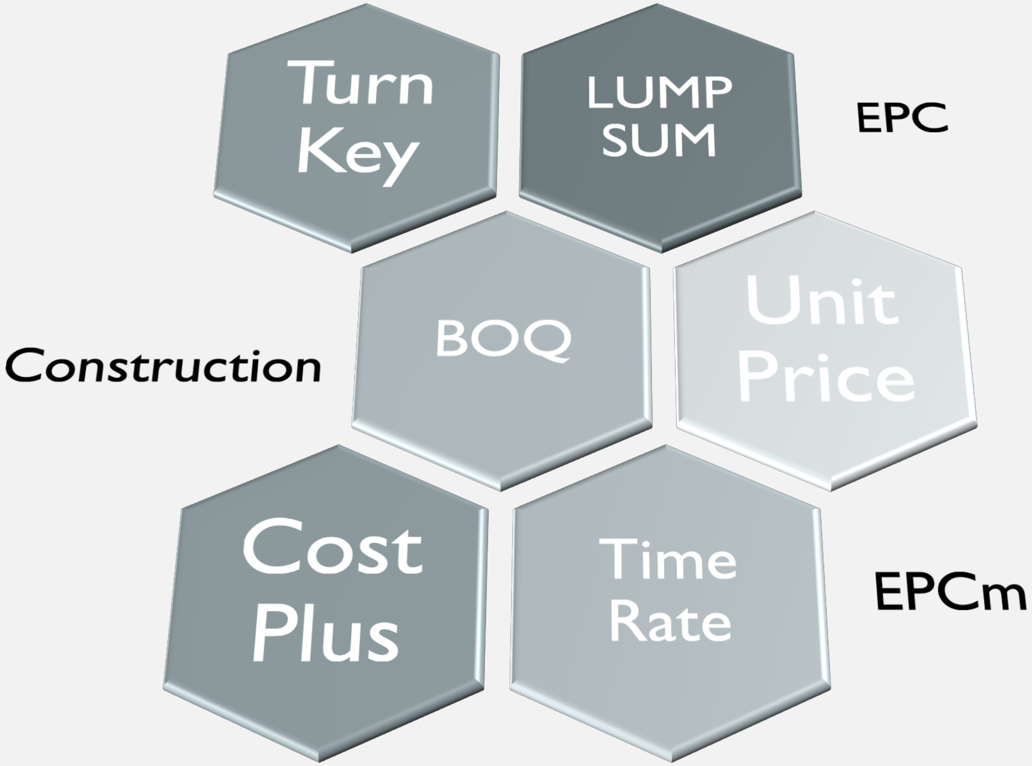
Engineering Contracts

EPC/EPCI/EPIC Contracts

EPCm Contracts

PMC Contracts

Construction Contracts



LUMP SUM FIXED PRICE

EPC, EPCI, , EPIC, C

Contracts

- The distinguishing feature of a lump sum contract is that the contractor is responsible for performing and completing the work as defined in the Scope of Work, for the fixed price stipulated in the contract.
- A successful lump sum contract requires:
  - precise definition of scope, quality of the deliverable and timing of work;
  - timely availability of Client supplied materials and / or services;
  - a well-defined and reasonable split of risk between Client and Contractor;
  - minimum scope changes and interference;
  - a detailed mechanism for agreeing the time and cost effects of changes e.g. schedules of rates for agreed extras.
- These requirements imply a significant amount of project planning and definition prior to the tendering and evaluation, and thus require a long lead time before an award can be made.

TURN KEY CONTRACTS

EPC, EPCI & EPIC

Contracts

including

Commissioning, Start-up & Testing

- A *Turnkey Contract* is a contract where the essential design emanates from, or is supplied, by the contractor, who therefore, to a large extent, also has the legal responsibility for the design, and performance of the work after completion.
- A Turnkey Contract is therefore not necessarily a lump sum contract, nor a contract with a single contractor for an entire project, although this is often the case.

BILLS OF QUANTITIES

EPC, EPCI, EPIC, C

Contracts

- Bills-Of-Quantities (BOQ) contracts are lump sum contracts with detailed bills-of-quantities (firm or approximate) forming a precise definition of the scope of work. BOQ contracts list all the quantities of work to be performed in a standard format and to a standard level of detail. If those quantities are stated to be firm then those are the actual quantities that will be paid for at the tendered rates regardless of whether those quantities actually turn out to be correct or not.
- The tendered rates are then, indeed, used solely to cost variations. However, a BOQ contract is usually more of the approximate type, where the actual quantities will be measured upon completion, and those agreed, final quantities will be the basis upon which the contract price is assessed. In this case the rates are used not only to value variations, but also to establish the price to be paid for the work.
- Payment under a bills-of-quantities contract may be on a monthly basis against measured quantities, or against a series of milestones. Milestone payments are preferred when the milestones can be clearly defined.

UNIT RATE / UNIT PRICE

EP, EPC, EPCI, EPIC & C

Contracts

- In unit rate/price contracts rates are fixed for specific items of measurable work and the contract price is then determined by measurement of the work actually performed.
- The prime characteristic of this type of contract therefore is that the overall quantity of work ("scope") is unknown at the time of contract signature, but the scope of work for each unit is defined.
- Its effective use does require, however:
  - sufficient project definition to provide a reasonable approximation of the scope of work and quantities involved;
  - coverage of all significant jobs within the agreed schedule of rates (additional materials, skills, or equipment may be difficult to negotiate after contract award);
  - clear definition of indirect costs included in the agreed rates;
  - caution in supplementing unit rates with day rates, which may result in contentious or even duplicate charges;
  - timely availability of Client supplied materials/services;
  - accurate measurement of the work as it is completed, on quantity as well as quality.

DAY (TIME) RATE

Offshore & Construction

Contracts

- Day Rate or Time contracts are types of contract where the major element of contractor remuneration consists of a fixed rate per day (or hour, month) for work performed. The day rate is a fixed price bid by, or negotiated with, the contractor.
- Day Rates occur usually in the context of a drilling or construction contract, with the main item of equipment or spread provided by contractor being a drilling rig, construction lay-barge, or similar pieces of major equipment.
- Under such contracts, as much as possible of the scope of work should be covered by unit rate contracting e.g. drilling a specified footage of a well laying a length of pipeline per specification, or mobilising the equipment to location.
- Day Rates apply in these contracts for those parts of the work:
  - *where the scope of work cannot be sufficiently defined to allow lump sum contractor remuneration;*
  - *where significant or unquantifiable risks are present which would be unreasonable or uneconomic for the contractor to carry alone.*
- Day Rate compensation is of two types:
  - *<u>Incentive:</u>*
The contractor has an impact on the quality of the product or service to be delivered, i.e. the contractor has an impact on the timeliness, scheduling, safety, technical performance.
  - *<u>Non-incentive:</u>*
The contractor has little or no impact on the timeliness and quality of the product or service to be delivered.

COST PLUS

E, EP, EPCm

Contracts

- The main characteristic of the cost plus / reimbursable cost type of contract is that the contractor is paid all direct and indirect expenditures he has incurred on the basis of actual cost without an overlay for profit. Usually, an incentive scheme is built into the contract, which provides the contractor with his profit if the criteria established in the Scope of Works have been met.
- Payment of the incentive occurs gradually over the life of the contract at specified milestones if, and only if, certain agreed project objectives (time, budget, quality and HSE) have been met. It is recommended to offer to increase the normal profit amount potentially available to the contractor with a substantial additional payment making together the so-called Incentive Fee. The number of milestones selected for release of the Incentive Fee during the life of the contract should be limited and the greater part or if possible all of the Incentive Fee should be available for potential release upon completion. Incentive Fee payments missed at any one milestone should be rolled over into the next milestone and ultimately to the completion date.
- The cost reimbursable elements should include only actual costs incurred. Fixed elements such as "percentages for overheads" should be avoided unless it can be established in advance that these do not offer niches for recovery of anything other than true costs.