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Project Management Professional (PMP)® Exam

Crosswind Success Series:
PMP® Exam Bootcamp Manual

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Version 6.1 aligned with the Project Management Institute, *A Guide to the Project Management Body of Knowledge, (PMBOK® Guide)* - Sixth Edition, Project Management Institute Inc., 2017

Contract Type	Risk for Buyer	Risk for Seller	Description	Example
Time and Materials (T&M)	Minimal	Minimal	The time and materials contract is typically used **for smaller initiatives, staff supplementation,** the initial piece of a project where discovery occurs before the full details of the project are known, or for materials on an initiative to complement the labor.	A buyer hires a technical writer at $75 per hour to supplement its staff or a buyer has a bathroom added to her house at $50 per hour plus the cost of materials.

15.1.8. Share

A share is a contract component that divides any remaining money (typically the difference between the total price and actual seller's costs) between the buyer and the seller. It is normally a negotiated split between the two parties. It is typically different from a traditional incentive fee in that an incentive fee pays compensation based on certain measurable performance metrics that have been established and agreed upon.

It is very important to understand and be able to calculate the total share and the amounts that will be allotted to the buyer and to the seller.

Example: The buyer and seller have contracted for the seller to provide a debit card add-on system in all 50 of the buyer's retail stores. The total price is to be $50,000. The need for implementation is great because the old systems are being leased and must be returned by a particular date. Both parties negotiate and agree that if the project's actual cost is below the baseline (target) cost, the buyer and seller split the difference 60%/40%. The project accrues an actual cost of $45,000 when complete. Calculate the share total amount and the share for the buyer and seller.

The project has a $5,000 share amount ($50,000 - $45,000). Of that $5,000, 60% goes to the buyer and 40% to the seller. The buyer keeps $3,000 and the seller gets $2,000. With the actual cost of $45,000 and the share amount of $2,000, the seller is paid $47,000 on the contract.

15.1.9. Point of Total Assumption

The calculation for the point of total assumption establishes the point in a cost curve where the seller's profit starts to diminish when taking into consideration the share ratio on cost overruns. As costs increase past the point of total assumption, a reduction in seller profit occurs until the ceiling price is met. Once the ceiling price is met, every dollar in cost results in a dollar loss for the seller. Contrary to what fixed-price may imply, a contract of this sort can be negotiated so that the buyer agrees to share in cost overruns or under-runs. This calculation is typically used in government or defense-type contracts.