MANAGEMENT CONSULTING SERVICES
Steve L. Wintner, AIA Emeritus

FORMULATING HOURLY BILLING RATES

Elements of the Hourly Billing Rate:	**Multiples**
1. Labor: Salary per Hour per Employee:	1.00
2. Payroll Benefits: Customary & Mandatory (as a % of Direct Labor):	0.35
3. Net Overhead: Indirect Expenses (as a % of Direct Labor):	1.20
4. Break-Even (B-E) Rate (1+2+3):	**2.55**
5. Profit: (2.55/.80) = $31.875 (for 20% Profit x $31.88)	0.638
6. Billing Rate (4+5):	**3.188**

Profit is calculated as a percentage of the Billing Rate, NOT as a markup of the Break-Even Rate. To calculate the Profit from the Break-Even Rate, you must divide B-E by the complement of the Targeted Profit. If the Target P rofit is 20%, divide B-E by its complement of 80%. The result is your Billing Rate.

Analysis by Example:

Assumptions:

1. Labor: $20.00 per hour
2. Payroll Benefits Factor: (Payroll Benefits÷ Direct Labor) = 35%
3. Net Overhead (Indirect Expenses ÷ Direct Labor) = 110%
4. Target Profit: 20% (1+2+3) ÷ 80%, the complement of the desired profit percentage

Where,

Billing Rate = Hourly Labor x (Benefits Factor+Net Overhead) +Hourly Labor + Profit,

then,

$20.00 x (35%+110%) = $20.00 x 145% = **$29.00 (Overhead Cost)**

and,

$15.50 + $20.00 = **$35.50 (Break-Even Cost).** This is the cost to the firm for a $20/hr. salary.

Then,

To add the Profit to the B-E Cost: divide the B-E Cost by the complement of the Targeted Profit %: $35.50 ÷ 80% = **$44.38 (Billing Rate)**

Therefore, for a $20.00 per hour salary, with a 145% firm-wide overhead rate and a 20% Profit included, the Billing Rate would be $35.50+$8.88 =$44.38 .

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To check:

Multiply the Billing Rate by the Targeted Profit % ($44.38 x 20%) = $8.88 Profit.

If you subtract the Profit from the Billing Rate, you get the Break-Even Rate ($44.38 - $8.88 = $35.50).

Comment:

If you were to multiply the B-E Rate by 20%, (which is a 'Mark-Up') instead of dividing its complement of 80%, you would get ($35.50 x 20%), or $7.10, which is $1.78, less than the Targeted Profit of $8.88 (or.$1.78 / $8.88 = <20%> less Profit)