



Bidding Projects Successfully

As the chief F.O.G. (F#@&ing Old Guy), I have learned that people tend to fight about two things in life -- sex and money.

In game development, everyone is too busy to be getting any on a regular basis, so it just comes down to money. And the most amazing thing I've learned is that, despite years and years of experience bidding projects, **a lot of people still set themselves up for a fight when they really can avoid it by changing their approach just a little bit.**

Last month, we talked about *the art of the RFP*

http://www.openmoves.com/accounts/FOG/issue_8_021508f.html#underhat, doing the right things to make sure you win a job. In that lesson, you learned that price is not the primary determining factor in the vast majority of selections.

In this one, we will talk about **why pricing can still get you into trouble after you have won the job if you did it incorrectly.**

How many times have you bid a project with a certain profit margin in mind, managed it closely, but still not ended up with the same margin once all was said and done -- and you wondered how it happened? Or you have cut your resource allocation close to keep the bid low, then watched your margin get gobbled up in the course of development -- and perhaps even lost money in the end, leaving you vainly hoping that royalties kick in 9-15 months later to save the ROI on the project? Or, even worse, you under-resourced the job to the point that your ability to deliver is in question and you have to go back to the publisher, hat in hand, and ask for more money absent significant design changes? **What do you think your chances are of getting repeat business from that company after that?** Or, as one of the owners of the studio, who is expected to take less when times are lean, you find that all of your team is compensated but you are working for minimum wage at the end of the day because there is nothing left for you?

Ladies and Gentlemen, that is not how to run a business. **Chances are, you have committed one or more of the following three common mistakes, all of which can be avoided ...**

Mistake #1: Passing on all of your competitive advantages to your customer.

Do you get wage subsidies or R&D tax credits from your government? Have you worked very hard to create an environment which attracts high-quality employees without the need to pay top dollar on your employment agreements? Do you have employee profit-sharing plans in place which allow you to pay smaller upfront salaries? Many developers enjoy one or more of these competitive advantages, **then turn right around and pass on all of that savings to their customers** because they feel they need to compete on price alone. When you do this, publishers benefit but you do not, which makes no sense.

If you get wage subsidies or tax credits of 40%, as some Canadian studios do, those wage subsidies are for you, to ensure the stability and growth of your company, not to ensure the stability and growth of your customer. Likewise, if you have a great guy that puts out a ton of work at 60% of the going rate for a person with his skills in the industry, and you bill him out unmodified at the lower rate, it might make you appear more competitive, **but you have cut yourself to the bone in the process.**

A better approach when trying to open a relationship with a new publisher is to pass on some, but not all of the benefit to your customer, and strike a balance between near-term profits and long-term competitive advantage. Once you are working with a customer and making them happy, it is usually easy to recapture in subsequent agreements any savings you passed on to them in the first agreement.

Mistake #2: Calculating your studio's man-month rate incorrectly.

I have seen this done countless ways over the years, but I have only seen one foolproof way to do it, and I am sharing that here. First, if you are not running your studio with an annual operating budget, spend the time and money to get one done professionally. If you don't, I assure you that you are taking all of your real costs into account when you bid projects **and your profits are suffering accordingly.**

Now, if you take the sum of all employee salaries and benefits and divide that by the number of employees, you come up with a man-month rate, **but it won't be the right one to charge.** For example, if you are an owner and you should be making \$120k per year, but you are only paying yourself \$50k in the budget because you expect to make up the difference on profits, you never will unless you make the appropriate adjustments now.

So step #1 is to use the salary and benefit figures you should be paying people if the studio is gainfully employed. Redo the annual average on that basis, divide by 12 and you will come up with an *unloaded man-month cost*, which is *just the beginning* of your calculation.

Step #2 is to take 100% of the rest of the operating budget of the studio -- and by that I mean everything that is not related to salary and benefit expense, from travel and trade show expenses down to paper clips and telephone charges -- and divide that number by your total headcount and then by 12. This will give you the *expense contribution* each employee must make via the billing you do on their services.

Step #3, add the unloaded man-month cost and the expense contribution. Now you ought to be able to add your profit margin and bid right? **Wrong!** That method would only work if your studio is 100% gainfully employed in paying projects throughout the year, and perfect project flow is a very rare thing in this business. If you have run your business for four or more years, you should have a really good feel for how much downtime you actually have and you can use that number in your calculations. If you don't have a feel for it, then use 20% as a modifier, so that's 1.2 x (unloaded man-month cost + expense contribution). This ensures that, as long as you are billing out 80% of the studio's capacity, you are not using your profit margin to fund the other 20% of your operational expenses.

Step #4, figure in your targeted profit margin. We will use 20% for our calculations here, so you multiply by 1.2 again the result of the prior calculation. This becomes your fully loaded *billable man-month rate*. For example, if you determine an average unloaded man-month cost of salary and benefits of 5000 USD, and an expense contribution of 1200 USD, with a 20% downtime allocation and a 20% profit margin (the rate which some

publishers even mandate in their contracts that you can take on upfront advances), then you come up with a billable man-month rate of \$8928.00. In other words, $(1.2 \times (5000 + 1200)) \times 1.2 = \8929.00 per man-month.

Mistake #3: Negotiating on man-month price, not on the scope of the project.

Once you have calculated your *billable man-month rate*, it should not become the basis of subsequent negotiation except as a method of last resort. It is your *cost* for each man-month that you build into the project. If your publishing partner is looking to lower the overall cost of the project, you need to be having the discussion on the basis of the scope of the project, not on the basis of your price for each man-month of development resources committed to it. **In more than 95% of the negotiations I do, any disparity between what the publisher wants to pay and what you need to do the project can be resolved in this manner.** And for the 5% of projects that still need to be adjusted, you have a 20% margin with which to plan, if necessary. Just remember that is a fair target for your company and you are in business to make money, not to work at cost. If you are dealing with a publisher who thinks you should work at cost or needs to keep their development advance to an absolute minimum because they overpaid on a third-party license, for example, you always have the option of doing a hybrid deal, making the advance non-recoupable and taking royalties from unit one to get your profits that way.

At the end of the day, both publishers and developers want to have manageable levels of risk, acceptable levels of potential return, and a safe ride in getting the product to market. As a developer, you should know your business more intimately than they ever will. **If you haven't taken the proper steps to plan, bid, and negotiate your studio's involvement in any potential deal, you are doing an injustice to yourself, your partners, and your employees.**

Underbid or under-resource a project and the publisher won't remember the 10% you might have saved them; they will remember the marketing spend and retail placements that were wasted. Underbid or under-resource a project and your employees usually won't even know why it happened, but as a minimum they will know that it wasn't a pleasant experience for them.

Bid smart, people, and may you also have the chance to bid often. And ... **Good Hunting!**