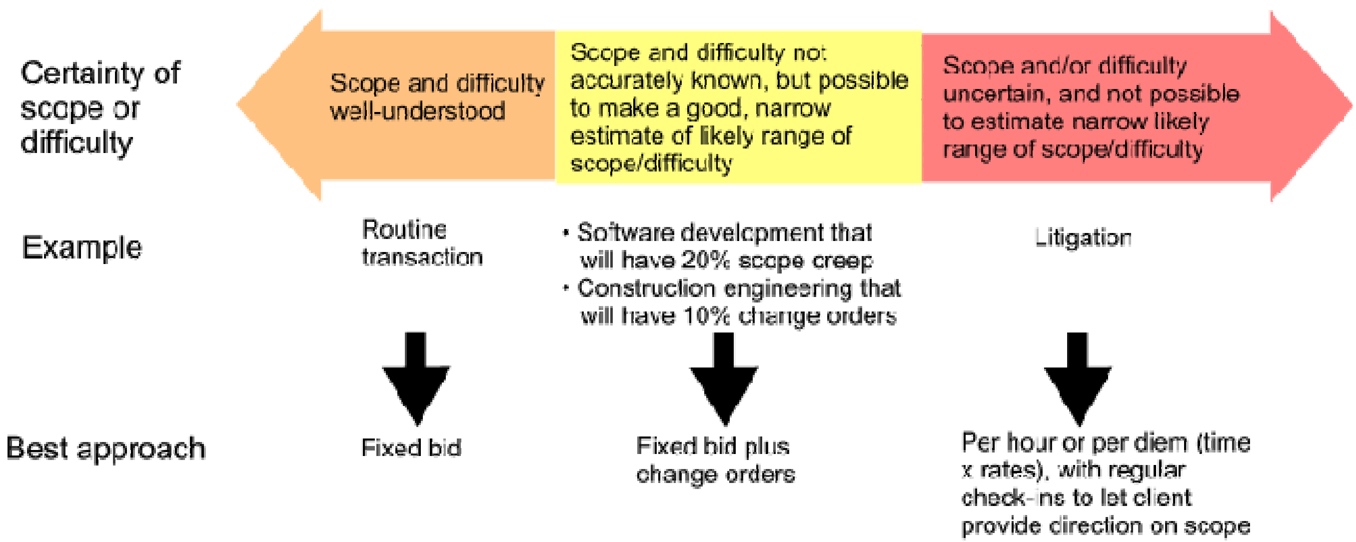
Pricing structures

Pricing is a critical business development skill. Your price level (how much you cost) and the structure of your prices (how you charge) both affect how easily you can get and keep clients. You might want to think about pricing structure to gain an advantage -- or you might need to if clients are asking for a different approach.

Different pricing structures hand risks to different parties

Pricing structures affect who bears two major risks in projects. *Uncertainty of scope and/or difficulty is the first risk.* Projects differ in how well their scope and/or difficulty can be predicted.

Spectrum of conditions regarding uncertainty of scope or difficulty of project



The second risk is poor performance: the risk that a professional will do an inadequate or incomplete job or be unexpectedly inefficient in completing the work. Clients face performance risk when they cannot easily evaluate what they might get, e.g., in considering off-shore custom programmers.

Fixed fees work when work is well-defined

You and clients both benefit from fixed fee pricing when the work is very well defined and the client knows well each firm they are considering. If you can do the work better than others, e.g., because your methods are better methods than competitors', you can beat other bids and still profit. Clients get a known price for the work, and can easily compare proposals.

If the clients aren't sure of the quality of all the firms, they'd be smart to only pay after defined project milestones are met, and to reserve much of the payment until completion. You should be happy to accept or even suggest such payment arrangements because they will discourage low-quality low bidders.

Per diem works when scope or difficulty is very uncertain

At the other end of the certainty spectrum, you and your clients both benefit from per hour or per diem pricing, as long as you and they regularly decide together how the project should proceed. This structure ensures you can bill for what you do, whether you end up doing much or little. Clients should also like this structure because it encourages professionals to lay out all the options at important decision points and lets the client pick the option the client wants.

If the client knows all the firms well, the client can estimate the relative prices by comparing hourly rates and adjusting for the known effectiveness of the firms (e.g., they might know that law firm X typically takes 20% longer than law firm Y for the same task, so they wants to factor in that difference). Firms can also justify their higher rates by suggesting or documenting they can do the job in fewer hours.

If the client doesn't know all firms well, they face a difficult situation. They can make quality assumptions based on references and even on what other companies who use multiple firms seem willing to pay. But they would also be wise to include in their plans stopping points where they can change firms. And they should do what they can, inexpensively, to preserve changing firms in mid-project as a viable option. If the client discovers they were wrong about the firm they picked, they won't have to live with that firm until the end of the (possibly very long) project. Again, you would welcome or even suggest this kind of stopping point to weed out low quality bidders who try to win by offering very low rates.

Middle ground is tricky

In the middle, the professional and the client may have different views of what will happen. The client insists there will be no changes ("we're sure our requirements statement is complete and correct"). They'll want a fixed bid to lock in a low price. You will expect scope creep, and prefer per diem. In these cases, consider encouraging the client to ask for a fixed fee bid to meet their written requirements, and a separate hourly rate for change orders. That way they get the best price on the part they know about, and you are protected in the (likely) event that there are changes.

Something to try this week

Think about the pricing structures that you prefer and what clients seem to be asking for lately. Consider these questions and actions:

1. If a client often wants a different pricing structure than you prefer, do you understand why? If not, think about asking them so you can find a mutually beneficial way to respond to their underlying concerns without taking on undue risk yourself.
2. Do you have an immediate opportunity to offer a new (for you) pricing approach in a proposal? Is there an approach that differs from your usual structure but improves your chances of winning the work and at the same time appropriately shares the risks between you and your client? Go ahead, propose it!

What are these tips?

These monthly tips are intended to help professionals create more business and enjoy their work more. We focus on how to start relationships, how to build relationships, and how to convert those relationships into sales.

Can you answer my questions about business development?

We'd be delighted. Please send any questions you have to questions@bridgewellpartners.com and we'll do our best to help you out. Or call us at 312-863-3489. Or visit www.bridgewellpartners.com to learn more about how we coach and train professionals to be better at business development and to enjoy it more.