

# CRACK THE PRICING CODE

Implement Value Based Pricing  
and Generate Fortunes



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“Hourly billing forces you to work long hours, creates negative cash flow, and puts you in the unenviable position of competing on price,” says Trivers.

Value based pricing compensates you for value, innovation and speed. High growth clients will pay handsomely for these and the opportunities are unlimited.

*Henry DeVries, contributor Forbes.com*  
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# Introduction

## The Catalyst

One August day, ten years into my consulting practice, I was sweating in my air-conditioned office. I was looking at a stack of June invoices for tens of thousands of dollars that were due to me for my work. I was also looking at having to pay out of my cash on hand the various current compensation and overhead expenses I'd incurred on behalf of clients. In effect I was extending uncompensated credit to Fortune 1000 companies and I hated that. They hadn't paid me for weeks after the work was completed. This happened time and again and my anger had reached the boiling point.

At that time, I was often hired to advise teams responding to federal government RFPs. They relied on me to provide insight into the requirements and to help them make their responses powerful and compelling. Hundreds of millions of dollars were at stake and every client felt the urgency to win.

They typically hired me, and all other outside advisors, on an hourly basis. I got paid for my time on site. This meant I could only

send invoices after the work was completed. They also insisted on 45-60 day payment terms. Accounts receivable would pile up while I'd have to pay my salary, expenses, and my subcontractors out of my cash on hand. Company cash flow was always negative.

On this particular day I realized I'd been unhappy and stressed about this recurring situation for years. Yet I accepted projects one after another knowing it would happen every time. This was the way every single other advisor I'd ever met did business. I wondered how could I possibly change this practice?

Something shifted in my brain that day: beyond the personal toll of the stress and uncertainty, this continuous negative cash flow put my company at risk. I knew that 82% of business failures were due to negative cash flow.

I decided in that moment that I must prevent that from happening to my company.

## **The Alternative**

I'd become familiar with the concept of value based fees: that clients should pay for our knowledge and expertise commensurate with the value to them, not for the time it takes to provide that knowledge and expertise.

The few proponents of value based fees I knew offered three reasons to adopt them:

1. It is the only ethical option. Charging by the hour is unethical. The client deserves to enjoy the benefits of

the knowledge and expertise as quickly as possible while the provider benefits from taking longer.

2. It is the only practice that recognizes variations in value. Value based fees are commensurate with the value delivered. Hourly billing does not relate at all to any value, only to time spent.
3. It makes timely receivables possible. Once an agreement is reached on a project and its associated value based fee, the invoice is sent, and the client pays within 15-30 days.

I knew changing to value based fees would be a monumental undertaking. I would be up against decades of hourly billing habits. I would be swimming against the strong tide of “we always do it that way” thinking. There’d be suspicions that I was hiding something, that they’d be cheated in some way. And, I didn’t have the first clue about how I’d calculate value to the client in order to offer my work for value based fees.

I had a lot of work ahead of me. I also knew my history of using my wits and grit to get hard things done and believed I could do it.

## **The Switch**

About 8 months after I decided to solve the mystery of value based pricing, I was ready to make the switch. I wrote with black marker on a large piece of paper “Value Based Fees from Now On.” I posted it above my desk.

An hour later the phone rang. The caller had been referred to me because his company was getting ready to bid on a 1.15 billion dollar contract and they needed my help. We had a very comprehensive conversation, and it was clear that we were both feeling I would be an excellent fit for this effort. He then asked me how I charged. I looked at my handwritten note, took a deep breath and said “I do my work for a fixed fee based on the value to the client. I can send you an outline of the project and the fee within 24 hours.” He said simply “That would be great.” And that’s the moment when I knew value based pricing was going to work for my company and for all professional and business services companies.

When I met Jerry a few years later, I knew I could help him. Within 10 months he would have banished negative cash flow forever and established his firm as the go-to firm for his market because his clients knew they got great value for a fee commensurate with that value. He told me often that he was loving two additional benefits of his switch to value based pricing: a lot more guilt-free time to spend with his child and more money to support expanding his company without borrowing.

## **Jerry’s Story**

Jerry woke up one day feeling quite anxious. While three months ago he had enjoyed abundant cash flow, on this morning he was anxious because the firm’s cash on hand was dwindling rapidly. This was a particularly brutal feeling that morning because the high volume/high revenue work he depended on, tax return preparation, wouldn’t begin again for 5 months. This was not new to Jerry -- it happened every year—but he had finally reached the point when something had to change.

It was understandable that Jerry felt this way because of the nature of tax return work. It's seasonal and people only care about getting their return by the required date. Not only that but given how his firm was primarily known as a tax return preparer it seemed almost impossible that there was a way to generate other revenue in the 7 non-tax prep months of the year.

As Jerry looked at himself in the mirror, he thought about a statistic he saw the previous day that made everything seem even more dire. He read that 82% of privately owned professional and business services firms fail due to negative cash flow. No wonder Jerry felt anxious. Negative cash flow is both a personal risk to the owner and a risk to the larger economy.

Jerry decided he had to act. "But what?" he wondered.

## **A widespread problem**

There are more than 4 million privately owned professional, scientific, and technical services firms in the US. They employ more than 9.4 million people and contribute 1.9 trillion dollars (2017) to the economy. These employees and this economic contribution are at risk when 82% of privately owned professional and business services/knowledge work firms fail due to negative cash flow. Financial capital is taken out of the economy, the unemployed have nothing to spend at other businesses and energy and creativity are lost.

At first glance, it seems that seasonality-related negative cash flow can be balanced out by adding other services that are needed in other seasons. That is not always possible, and even if it is, it doesn't address the true cause of negative cash flow.

**The true cause of negative cash flow** is related to two practices that are pervasive in professional and business services firms:

1. selling deliverables (tax returns, plans, reports, classes, legal forms, and litigation)
2. charging for the time it takes to do the work that produces these deliverables.

*The belief that time is money is killing opportunities for more business, positive cash flow and long term growth.*

I have done proprietary research with over 300 professional and business services firms over twelve years and in 85% of companies, the prevailing belief is that charging by the hour is the only pricing model that works. There are 5 reasons cited most often to justify the practice, but when investigated they do not hold.

## **The Echo Chamber**

The drum beat of “best practices” promulgated by their various industry organizations and associations adds to the beliefs of the owners and executives of these firms. When revenue generation is addressed at all it is always as “How do we set our prices?” They make recommendations such as: research the competition to ensure that a company is within range of their competitors; or to price below competitors to try to gain a larger share of the market. Other advice relates to the level of skills needed to do good work (not great or outstanding work), meaning that salaries can be lower, which allows the firms to charge less. The firms I researched often were told by their accountants to cut expenses in order to set competitive fees. Accounting firm owners also believed this.

As companies extend their longevity, they ask “How do we raise our rates or our fees?” Among the advice my subject companies got was do it periodically according to a set schedule, add another service, win industry awards for excellence so clients would be willing to pay more, and keep up with the competition. Sometimes the advice was to tell clients their fees would go up and they could accept them or find another provider.

If you're recognizing these and have done them, remember, you are not alone. I spent ten years immersed in the myths of time is money and hourly billing.

It takes extreme effort to crack the code of value based pricing, overcome these engrained beliefs, commit steadfastly to a new way of thinking, and implement the new practices required by that new way of thinking.

I always remind professional and business services firms that:

**The key to generating fortunes is not by believing that time is money but rather believing that money represents value delivered.**

### **What did Jerry do?**

Jerry had heard me speak about my passion--how professional and business services firms can create dramatic growth-- and he gave me a call. I'll never forget his grim look when I entered his office. I knew he was normally a pretty cheerful guy, but clearly something was weighing on his mind.

He showed me his cash report from that past three months. The outflows were steady, the inflow was sporadic. I got the point immediately.

I was curious why he felt so differently this year since the seasonal fluctuation in revenue happened every year. He told me that his little boy, then aged 4, was starting to play T-ball and play with friends and he wanted to share those times with him. But he felt guilty because every hour away from the business was an hour he wasn't billing. And the company needed him to bill hours in order to have even a small amount of revenue coming in.

We had a deep and open conversation about the business. Jerry was a well-established and highly regarded CPA. **He knew the problem wasn't about his expertise. It was about his life.** He could not see any options and he asked for my help.

The first thing I did when Jerry asked for my help was to come to agreement with him on his wants and needs and what outcome would help him get those wants and needs met. We agreed on a 3-month effort with a clear scope of work and a value based fee.

This was his introduction to the concept of value based pricing—that money is compensation for value delivered, not for time spent. He would come to appreciate this more and more as we worked together.

We did some data gathering and analysis to understand his revenue streams and clientele. He had many longtime clients who relied on him for both business and personal tax returns. There was some revenue from bookkeeping services and some reports. When a client needed some advice, Jerry would meet

with them, give the advice and charge for the time. Every bit of revenue came from hourly billing. They billed different rates depending on which of his staff did the work. Billing was always after the fact, with 30 day terms.

I was surprised when Jerry told me that he had never suggested to his clients that he could help them with the financial management and decision-making of their companies and even some of their personal finance. He saw himself only as their “tax guy” even though in doing their taxes for years, he had a lot of knowledge about their businesses and could provide deep insight on their financial situations. He said no one had asked him, and he didn’t offer.

Once we understood the existing situation, we created a plan. My advice is to start with a well-defined initiative: not too big, and yet big enough to give some meaningful data. Once I understood Jerry’s range of expertise and the value it offered to meet the wants and needs of his clients, we designed an advisory package. We constructed three levels and each one included the tax return the clients counted on.

Jerry made a list of his top 32 clients and personally invited each of them to an after-work happy hour. He wanted to thank them for their longtime allegiance to the firm and he brought in a speaker on an interesting topic. 25 people came and the evening was enjoyed by all. During his remarks Jerry mentioned that he’d been thinking about ways to serve them even better and he would be meeting with each of them to share his ideas. After several weeks of meetings, 23 of the original 25 chose one of the packages.

The key to his success: he asked them about their needs and wants (beyond tax returns) and was going to help them get what they wanted for one fixed, value based fee, paid in monthly installments. They would have unlimited access to him during normal business hours and he'd prioritize their work and their tax returns. They were excited to be among the first to benefit from Jerry's new value based services.

As he steadily progressed with Value Based Pricing he reminded himself of the "bad old days" -- no time with his son, guilt when he wasn't doing billable work, how hard it had been to increase revenue, the sight of the dwindling cash report.

He remembered how deeply he had bought into the draining belief that time is money.

Now he knew, without a doubt, that the real way to ensure positive cash flow and increase profit is to **believe that money represents compensation for value delivered**. The bundled packages he offered to his clientele provided extensive value to the clients and continuously generated positive cash flow for his firm.

What were a few of his value based innovations? For one, he invested in cloud based software and automated, secure access to all clients' data. The firm set up schedules with clients based on the client's workflow to produce various reports from that data and deliver them as desired to decision-makers. He projected tax returns each quarter before estimated taxes were due, to help clients make the right payments. No overpayments or underpayments that would bite them months later.

It didn't matter how much time this took, it only mattered that these services met the wants and needs of the clients and they were more than willing to pay for them.

## **When Your Firm Offers More Art than Numbers**

What's the value of conflict resolution?

When conflict is raging within a company or organization, how they deal with it will make the difference between survival and extinction. One client is an expert at the art of conflict resolution. Make no mistake, conflict resolution between hostile people requires deep knowledge and expertise in human behavior, language, body language and the skill to reach an agreement that leaves the parties feeling better.

How can one possibly put a dollar value on an hour of this expert's time? If the resolution process and solution save an organization or company and it takes one hour to achieve, should that person be paid a few hundred dollars 'for their time'? And if it takes longer because people are often deeply invested in their position and take a long time to consider alternatives, should they be worried about the clock?

My client has 30+ years of experience and hundreds of successes under her belt and felt that she was often struggling to get compensation that represented the extreme value of her deep knowledge and highly tuned skills. I helped her crack the pricing code. We worked on a list of typical wants and needs of people in conflict and the value to their organization or companies of meeting them. She can document that her work could make the difference between a

company that makes millions of dollars and one that disintegrates because key parties failed to resolve their issues.

I reminded her often that believing time is money hurts all parties and that believing money is compensation for value helps everyone.

She agreed to transform her pricing approach from hourly billing to value based pricing and gave herself 6 months to make the change.

She changed the way she explored issues with prospective clients, focusing on the outcomes of resolving the conflict, rather than on the process of reaching a resolution. Once she started this practice it became easier for her to focus the prospective client on the benefits to them and on how her fee was compensation for those benefits, not her time.

For example, a non-profit was experiencing staff disagreements and threatening morale. Staff in-fighting would weaken the organization's ability to serve its clientele and donors. Resolving the conflict allowed them to maintain their donor base and fulfill their critical mission. In another instance, a private organization was being torn apart after decades by competing leadership factions. They had to either resolve the issue or disband. There was a lot of passion on both sides. With her careful, thorough, and well-executed work, they resolved their issues and more than a year later report that they are functioning normally, thanks to her.

Within a half year, she was using value based pricing and doubled her company's revenue while garnering even more accolades from satisfied clients.

## **The Failure of Conventional Wisdom**

As wide-spread as is the belief that time is money, it is an example of how ‘conventional wisdom’ is only conventional but not actually wise. Do you really want to adopt the conventional wisdom of people who struggle to create positive cash flow and fail to generate fortunes? I am dedicated to rebutting that conventional wisdom with real wisdom: money is compensation for outcomes not time.

*Crack the Pricing Code: Implement Value Based Pricing and Generate Fortunes* is the complete story of avoiding the epidemic failure of hourly billing and replacing it with Value Based Pricing. Every professional and business services company can enjoy the kinds of success Jerry and the 300 other client companies have enjoyed.

## **This Book is For You If...**

This book is for any professional and business services company who wants to meet financial goals beyond what they are currently achieving. It's for Owners, Partners, Founders and Executives of knowledge work companies including CPAs, lawyers, designers in all fields, architects, consultants, education and training providers, niche expertise providers, and any other company where knowledge and expertise is the main source of value to the buyers.

You can define ‘fortunes’ however it's meaningful for you. Comfortable, rich, no worries, great wealth. It's your life and your choice. *Crack the Pricing Code* is about achieving more than just getting by.

I use the phrase ‘generate fortunes’ to make the point that hourly billing does the exact opposite. Hourly billing decreases your ability to grow and it keeps you handcuffed to the failed idea that time is money. There are a fixed number of hours in a work week. Even if you sell all your available hours, and price them high, you can never bring in more revenue than the hours in a week. If you have unsold hours, you can’t even make the maximum. If you provide extraordinary insight and expertise that delivers fantastic value to the client, you make the same as the person who delivers average insight and knowledge. And you can’t reasonably raise the hourly rate because what changes? An hour is 60 minutes, period.

As Jerry and others have discovered, Value Based Pricing leads to other benefits beyond more revenue. When you don’t have to scramble to sell your inventory of hours, you are free to:

- Develop new services for your best clients.
- Invest in relationships.
- Spend more time with family and friends’ time.
- Support philanthropic efforts.
- Accumulate cash for expansion or growth in other ways.

Cash accumulated in the company is the cheapest way to finance growth. And it puts your company in the position to get great terms from lenders if you do decide that borrowing makes sense.

## **This Book Serves Two Kinds of Readers**

If you’re impatient, lacking time to read the whole book, or just want to get started revolutionizing the way your company does

business, read Chapter One. This bottom line upfront chapter conveys the highest level concepts of Value Based Pricing for privately owned professional and business services companies. You'll find the 5 Steps to CPC in this chapter as well.

If you're a deep-dive kind of reader, and read the whole book, you'll find everything I've learned since I cracked the pricing code for my company and from working with 300 companies on their implementation of Value Based Pricing.

*Crack the Pricing Code: Implement Value Based Pricing and Generate Fortunes* shows you how being compensated for value supports creating more value. No more worries about whether you have time to innovate and improve. Because your time is not money you can use your time for deepening your knowledge and expertise. You can use your time to enhance offerings and create new ones. You can decide to up level everything you offer because you'll be compensated for that. You can stop worrying about the competition. No competitor can offer the value that you and your team create. This recalls Oscar Wilde's saying, "Be yourself, everyone else is taken." Value Based Pricing allows your company to fully be itself and no one can copy you, steal from you, or undercut you.

Keep reading to learn that the real way to generate fortunes is to **believe that money represents compensation for value delivered.**