How To Raise Your Prices The Right Way

8 min read

I always say **the single number one decision that a business owner will make to increase profits is to focus on pricing.** For a small business owner, this can be a tough decision to make and may come with some concerns for your business.

Key Takeaways

- **Do The Math:** If you're running a company that has $10MM in revenue with 10% profits and you increase your pricing by 10%, assuming no decrease in unit sales, you'd increase revenue to…
- **Start By Considering Two Main Factors That Affect Pricing:** Before any work begins for the client, you must expressly state what is, and is not, included in scope and what the potential extra fees could be…
- **How do you do that:** If your business is supposed to have a 20% margin and you really only have a 12% or an 8% margin, then you can go in there and look at those extra costs**…**

"If you've got the power to raise prices without losing business to a competitor, you've got a very good business. And if you have to have a prayer session before raising the price by 10 percent, then you've got a terrible business." – Warren Buffett

What Do You Fear?

- Angry Customers?
- Losing customers to competitors?
- Going out of business?

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Do The Math

It's worth considering how a nominal increase in pricing can cause a material improvement in profits.

If you do the math, you'll see that just a 10% increase in price can translate to a 100% increase in profits.

If you're running a company that has $10MM in revenue with 10% profits and you increase your pricing by 10%, assuming no decrease in unit sales, you'd increase revenue to $11 million. You had $1 million in profits, now you have $2 million in profits. By increasing your pricing 10%, if you had a 10% profit, you're going to double because all that extra money goes right to the bottom line.

A lot of business owners say, "My price is set by the market. I can't just arbitrarily increase my prices 10%," and I say, "You're right. If your business is a commodity, that is 100% correct. You cannot increase your prices willy-nilly." However, if you are in the knowledge business and if you are a business that makes money on knowledge workers, skilled blue-collar or white-collar businesses - **In order to increase your prices, what you have to do is demonstrate all your value.**

What I find when I speak to CEOs is they are almost unanimous in their agreement that they are giving away value for which they are not getting paid. Most of them say it happens every single day. We had that problem. Why? Because service providers, in our case accountants, seek to please. They seek to get satisfaction from their work, which is shown in a happy client. Typically, service providers abhor sales. They don't like being sold and they don't like selling anything. They're engineers, they're IT support, they're accountants. They're knowledge workers.

It happens when a client asks for something, the service provider's first immediate reaction is, "Sure. We can do that," and just do it or give it away without any update to the original scope, especially if you're on a fixed fee.

Start By Considering Two Main Factors That Affect Pricing

1. Clearly Defined Scope Document

The best run companies have clearly defined scope in their contract and in the sales process. Before any work begins for the client, you must expressly state what is, and is not, included in scope and what the potential extra fees could be. By providing that in the contract upfront, you are making it clear that when a client asks for additional work, you can reply, "Yes, we can do that, but that's out of scope. Would you like me to submit a change order to take care of that for you?" The client is happy to pay it because they knew it going in.

Your scope document has to say what's included, what you get and what you don't get, and what things you may get charged extra for. Once you do that, the service providers of your organization are no longer sales reps having to overcome an objection. They are agents of change. They're happy to give you a change order because it fulfills their higher purpose, their self-actualization around service, and they want to serve you, and the more change orders that you agree to, the happier you'll be — because you’ll be getting exactly what you need.

2. Complete Visibility Into Time Spent

The second magic bullet here is you must have complete visibility into what you and your staff are actually doing every single day for your clients, and have a system for surfacing changes in time spent. **It's only when you actually see where the time goes that you understand the value that you're giving and you can monetize it.**

How do you do that?

If you have your time tracked in an app like TSheets® - and you are syncing that with your payroll, and allocating the labor cost based on the actual time being spent - you can get visibility into where there are things being delivered that are not in scope. So you'll be able to capture that value and learn from it.

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Here's an example: An IT company continues to get calls from certain clients, and those calls take an extra 15 or 20 minutes per day. If your employees are doing their best to approximate how much time they spend a day, then what you measure is how the actual time differs from what you budgeted for, what you thought it was going to be when you created the proposal?

If your business is supposed to have a 20% margin and you really only have a 12% or an 8% margin, then you can go in there and look at those extra costs. You should have visibility into your missing costs - your benefits costs, and your direct labor costs or extra time not charged that may be missing - e.g. for project managers, travel time that you're paying for that wasn't included in a bid, revisions to project plans, etc.

Then make a decision to either go back and renegotiate with your clients based on what they're actually getting, or terminate those old clients and replace them with higher margin new clients. You will be able to see the value and you can explain that value to the client, so they are willing to accept the increase, based upon added value.

"...A company exists only as long as it earns a profit and it can only do that if it delivers a quality product or service at the right price. This means that the key to any conversation about raising the price is to emphasize that such an increase will ensure product quality."

- The Balance

If they're not willing to pay for it, you can stop doing it. And then in effect, that's not the same as increasing your prices, but it does have the same kind of material impact on your profits.

If you're giving away services that you didn't think you were going to be giving away, then you either get people to pay for it or stop doing it.

This is a well accepted process because it's putting the decision in the hands of the client. "What would you like us to do? Would you like us to increase our fees by X% or would you like us to stick with the terms of the existing contract and stop doing this out of scope work?"

This process will have a huge impact on your profits. What we have found when we have gone in and helped our clients get visibility into their true labor costs and their true out-of-pocket costs is, if they deliver good value, if they have good service providers, if they have good relationships with their clients - - then they've been able to go back to their clients and renegotiate the deal. And you will be able to as well.

We helped one of our clients realize this, and they went out to their clients with a true expanded scope and increased pricing. Their clients came back to them and said, *"We love your company. We would rather pay more to a company that we know is going to deliver great services than save a couple of dollars and have risk of failure to deliver."*

The client told us, *"It took us a while to do that because we were afraid we might lose clients, but in reality we didn't lose any."* Within one year after hiring GrowthForce, **they went from breaking even to $1 million in profit because they changed their pricing.**

It’s important to have a very structured process. Take your scope document, do an analysis of time spent over six months, identify what the actual amount of time was by area of scope, and work being done that was not included in the original bid.

Show the client three options:

1. What it would take for you to continue to do the work that you're doing now
2. What would you stop doing if they stick to the original scope documents
3. What pieces of the work that you're currently doing right now that the client could do in-house so you would not have to increase the fees

Option One

"Here's a new increase in cost for the increase in scope."

Option Two

"Here's a decrease in services if you want to keep to the original fee," and the third, "Here's a hybrid. Here's how we can minimize the amount of our fee increase by having you do certain things that are inefficient and low value for us to do."

Instead of worrying what your clients will think, highlight all of the value they are getting. Understand your fully loaded labor costs and raise your prices the right way to increase your profits holistically.