HOURLY BILLING IS NUTS

ESSAYS ON THE INSANITY OF TRADING TIME FOR MONEY

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Essays On The Insanity Of Trading Time For Money

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Yours,

—J

To Erica, Cooper, and Maggie

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Introduction

Welcome!

For the past fifteen years or so, I've been an active participant in various software development communities. I've written four software books, I've spoken at hundreds of events all over the world, and I've maintained open source libraries used by tens of thousands of developers. I've hosted talk shows, meetups, and podcasts. And of course, I've been involved with hundreds of software projects for clients of all shapes and sizes from bootstrapped startups to Fortune 500 companies.

Suffice it to say, I chat with *tons* of software developers. I have found that whenever one of these discussions turns to the financial aspects of a software project, virtually everyone tells me that they bill for their work by the hour. I'm strongly against this practice because:

Hourly billing is bad for your business, your clients, and your projects.

I realize that most people bill for projects on an hourly basis. I also realize that with enough discipline, it can seem like it's working. However, it's an outdated practice born of cost accounting and factory management that was never meant as a means of setting prices for professional services. As far as I can tell, it only lives on through inertia.

If you disagree, let me ask you this:

When did you decide to start billing by the hour?

Never, right? Most people never consciously decided to bill for projects by the hour. In fact, they don't give the question any thought at all; they usually just jump straight to "how much should I charge per hour?"

The unconscious acceptance of hourly billing as the best and only option literally keeps me up at night. In fact:

I consider it my mission in life to rid the earth of hourly billing.

This is not just an issue for software developers. I've helped a wide range of disciplines escape the insanity of hourly billing: designers, copywriters, illustrators, photographers, accountants, lawyers, and more. The stories in this book are mostly all from the software development world, but it is clear to me that the underlying principles are valuable to a wide range of professional service providers.

With my mission in mind, I am publishing this book of my essays on the subject. It is my sincere hope that it will help you convince your colleagues, your clients, and maybe even yourself that hourly billing is nuts.

Let's get started…

Backstory

In my early thirties, I was making a little over $90,000 USD annually as the VP of a boutique software development firm. It was a good company and I loved my fellow employees, but I was miserable. I spent most of my time arguing about invoices with clients, hounding developers to log their hours, and responding to RFPs with estimates that almost always turned out to be too low.

Then one day everything changed.

In a flash, I saw with total clarity that billing clients by the hour was hurting me, my company, and our clients. It was the source of just about every problem that we faced as a company. Simply put, hourly billing is corrosive to client relationships across all professional services. This includes "digital" disciplines like graphic design, user experience design, copywriting, software development, and so on. You can't truly partner with your clients if you're billing by the hour, which means that you can't do your best work.

Here are five reasons why this is true:

1. Billing by the hour implies that you will first provide an estimate of the hours required to complete the work. This means that the buyer has to make a purchase decision based on an estimate, not a known cost. If the estimate turns out to be low then things get ugly

fast. Even if the client doesn't blame you for the overage, they will experience buyer's remorse because they spent more on the project than it was worth to them.

2. Billing by the hour encourages you to invoice in arrears (i.e., invoicing your client AFTER you've done the work). This puts you at the mercy of the client, usually on a weekly basis throughout the course of a project.
3. Billing by the hour allows you to "get to work" before the client's actual desired outcome has been identified. It's a classic example of "Something must be done! We're doing something! Something has been done!" Consider this: If you don't have a goal, you can't succeed. If you can't succeed, you must fail. If you fail, your client will be sorry they hired you.
4. Billing by the hour punishes increased productivity. If you are billing by the hour, you have a subconscious incentive to NOT become more efficient. Because of this, your skills will stagnate and your clients will suffer.
5. Billing by the hour creates bureaucracy. You fill out your timesheets. You send your timesheets to the client with your invoices. Your client has to review your timesheets and approve your invoices. Your client may ask (or demand) to discuss perceived discrepancies from one timesheet to the next. None of this activity produces a beneficial outcome for either you or your client. It's a complete waste of time.

Having had this epiphany, I just couldn't continue working by the hour so I left to start my own firm. Within a year, I had doubled my income. More importantly, I had drastically increased the quality of my work life. I was not tracking my hours, I was not working 60-80 hour weeks, and I was not debating invoices with clients (in fact, I rarely had to send invoices at all).

How I Realized that Hourly Billing is Nuts

In 2005, I was managing a small software development firm that built custom workgroup software. At the time, we had 10 developers and billed projects out at $150/hr. The most senior developer was a guy who I'll call Fred, and the most junior was a guy I'll call Barney.

Fred wrote elegant, bullet-proof code and he did it fast. He was totally self-managed, fun to be around, and had stellar customer satisfaction numbers. We paid Fred $90k per year.

Barney was just starting out in the industry, and as such, he wrote a lot of spaghetti code and it took him a long time to do it. He needed a lot of attention, encouragement, and training. Although he wasn't the greatest coder, he was very personable and kept his customers quite happy. We paid Barney $45k per year.

At a certain point, money got really tight and we had to consider every alternative, which included the possibility of letting someone go. Fortunately it never came to that, but the situation did reveal a bizarre truth:

If we fired someone, *it would have to be Fred.*

This was completely counter-intuitive because we were in the business of writing software and Fred was better at writing software than Barney. In fact, Fred was better at writing software than anyone I'd ever worked with and we were lucky to have him at all.

However, Fred was fast and expensive. He burned though projects so quickly that we sometimes couldn't get new clients fast enough to keep him busy. And when we did have work for him, he would bang it out quickly and efficiently.

Barney, on the other hand, was slow and cheap. Once, we gave him a project that would have taken Fred two weeks, and Barney was still billing hours against it six months later. We were paying Barney half of what we were paying Fred, but Barney was bringing in steady money from a single client, and for a long time.

I just couldn't reconcile this situation; I knew something was wrong. My head told me to keep Barney, but my heart told me to keep Fred. After weeks of struggling with this puzzle, I was eventually forced to question the underlying assumptions of the business. And that's when the light bulb went on:

Billing by the hour was the source of virtually every problem our firm was facing.

Sure, hourly billing was (and is) the norm with my colleagues and the expectation of my clients. But just because everyone does it doesn't mean it's sane.

Billing by the hour is just as bizarre as billing by the pixel, or by the line, or by the color. *They are all arbitrary units of measure that have nothing whatsoever to do with the outcome of the work.*

I know you're probably thinking, "Er… no… hours are different because that's my TIME… and pixels or lines or colors, those aren't my time… and time is money… and something, something…"

I get it. This is hard to wrap your head around. But stick with me. Suspend your disbelief. Keep an open mind and the benefits will be life-changing.

The Moral Dilemma of Hourly Billing

Imagine that you've estimated a 40 hour job at $200/hr for a total of $8000. The client happily approves it and you rejoice.

After some initial research, you discover that there is a tool available for $1000 that will allow you to deliver the project in 5 hours, rather than the 40 hours that you've estimated. What do you do?

A) You buy the tool for $1000, you deliver the work in 5 hours, and bill the client for 5 hours. Result: You work 5 hours, pocket $0, own the tool, and the client loves you.

B) Have the client buy the tool for $1000, you deliver the work in 5 hours, and bill the client for 5 hours. Result: You work 5 hours, pocket $1000, the client owns the tool, and the client loves you.

C) You buy the tool for $1000, you finish the work in 5 hours but wait to deliver it at 30 hours, and bill the client $6000. Result: You work 5 hours, pocket $5000, own the tool, and the client is very happy that you finished faster and cheaper than promised.

D) You don't buy the tool, you deliver the work in 40 hours, and bill the client $8000. Result: You work 40 hours, pocket $8000, don't own the tool, and the client is satisfied.

I think that all of these options suck, and I don't advocate any of them.

What's interesting to me is the moral dilemma between C and D. C is clearly dishonest, but it's undeniably better than D for both you and the client. The client saves $2k, receives their work 10 hours earlier than expected, and you make $1000 per hour!

I can imagine a variety of other options, and I'm sure you can, too. Unfortunately, none of them would address the underlying issue: that **billing by the hour for software projects makes no sense.** Software projects should be billed based on the client's perceived value of the outcome. Period. How many hours it takes you to deliver it is irrelevant; in fact, the fewer the better!

Hourly Billing Punishes Increased Productivity

When I first switched to value pricing for software projects, I was struck by my sudden inclination to research and purchase tools. These days, I don't think twice about dropping $500-$1000 for something that will make my work go faster or better.

Herein lies an insidious truth about hourly billing: If you are billing by the hour, you have a subconscious incentive to NOT become more efficient. Because of this, your skills will stagnate and your clients will suffer.

Hourly Billing Prevents Growth

Technically, I shouldn't care if software consultants bill for projects by the hour. If some software consultant wants to do themselves - and their clients - a disservice by charging hourly, it gives me a competitive advantage. **After all, clients don't buy hours; they buy results, which is what I sell.**

While this line of reasoning might make sense in the short term, it's deadly in the long term. Here's why:

A software consultant who bills by the hour has no financial motivation to build or purchase tools that would save time, to participate in professional development, or to stay on the cutting edge of industry research. In short, they have no incentive to get better at what they do.

When an entire industry consists of people operating in this manner, there is little hope of progress for the group. No one will forge ahead in a groundbreaking way because there is a financial disincentive to becoming better at solving problems faster.

Therefore, an industry that bills by the hour will never get any better at what they do.

I find this realization both depressing and ironic, considering that everyone in this business despises inefficiency. Hopefully, you agree.

Hourly Billing Hurts Software Projects

Over the years, I've worked with a lot of software consultants. The vast majority of them follow a project lifecycle that looks more or less like this:

1. A client (let's call him Bob) needs something built (a web application, for example).
2. Bob contacts a consultant (Alice) because he knows that she builds web applications.
3. Bob and Alice discuss the application until she feels like she understands it fairly well.
4. Bob asks Alice how much it will cost to have her build the web app.
5. Alice estimates that the project will take around 100 hours, she multiplies that by her $200 hourly rate, and sends an estimate for $20k to Bob.
6. Bob approves the estimate, and Alice starts working.
7. Alice keeps track of her hours while she is working. For each time entry, she includes a description of what she did.
8. Alice sends an invoice to Bob every Monday for the hours worked in the previous week. The invoice includes a list of the hours worked with descriptions.
9. Bob reviews Alice's hours and pays her invoice.

Steps 8 and 9 repeat until the project is done.

Two Problems of Hourly Billing Process

I want to call out two of the problems inherent to this process:

1. Administrative overhead for Alice

Alice is spending up to four hours every week tracking her hours, preparing an invoice, and processing payments. If she has two or three projects going at the same time, she could be losing more than ten hours per week to administrative duties.

2. Bob will start questioning hours

Sooner or later, Bob is going to start reviewing Alice's hours. This typically manifests itself with questions like, "Why did it take two hours to run the data import last week, when it only took one hour the previous week?" Addressing these questions can be a big time suck for both parties, and it adds no value to the project. **More importantly, it creates a trust fracture between the two parties.**

This behavior usually becomes more pronounced as the actual hours approach (or exceed) the estimated hours. If the web app isn't done and Alice is 50 hours over estimate, Bob is going to become really irritable. In this situation, he'll probably go back over every invoice looking for inconsistencies or items that he feels shouldn't have been charged for.

It's a vicious cycle - more time is wasted debating about hours, mutual distrust is increased, and the project is further delayed.

How to Fix the Problems of Hourly Billing

Most software consultants try to solve the inherent problems of hourly billing by optimizing the process. They think the solution is to use better time-tracking software, or to integrate their CRM with their accounting system, or - my personal favorite - to bill clients hourly for time spent resolving disputes about hours.

It is true that optimization can make these problems less bad. However, optimization treats the symptoms and ignores the disease. **The real way to solve the inherent problems of the hourly billing process is to stop billing software projects by the hour.** When a project fee is based on the perceived value to the client rather than the hours of the consultant, the issues listed above simply evaporate.

A software project is a goal-oriented, ongoing collaboration between client and consultant. A project can't be a true success for both parties without this mutual trust. Mutual trust is the natural result of the two parties sharing in the risk (and reward) of the undertaking. Value pricing creates a shared risk/reward environment.

Hourly Billing Is Hurting You and Your Clients

Why question the logic of hourly billing at all? It's what your clients expect, right? It's how your competitors do business, right? Not to mention other professional service providers like lawyers, accountants, and psychiatrists. If it works for them, why won't it work for you?

I'll tell you why: hourly billing is corrosive to client relationships across all professional services. This includes digital disciplines like graphic design, user experience design, copy writing, software development, and so on. You can not truly partner with your clients if you're billing by the hour, which means that you can't do your best work, which means that your clients aren't loving you as much as they could :-)

There are lots of reasons why this is the case. Here are a few:

1. Hourly billing misaligns the direct financial incentives between you and your client (i.e., the longer the project takes, the better it is for you and the worse it is for the client). This creates trust fractures which erode the relationship over time if your estimates are not accurate. This erosion manifests itself as questioning hours, micromanagement, and lack of testimonials/referrals.
2. Hourly billing allows you to get started before knowing your client's goal. It's a classic example of "Something must be done! We're doing

something! Something has been done!" Consider this: If you don't have a goal, you can't succeed. If you can't succeed, you must fail. If you fail, your client will regret their decision to hire you.

3. Hourly billing discourages you from becoming more efficient. On one of my first value based projects, I found myself shopping around for plug-ins that might help me complete the project faster. I found one that did just what I needed. It was $700 - which was more than I had ever spent on a piece of software - but it saved weeks of development time which directly benefited both me and my client. Had I been billing by the hour, *it wouldn't have even occurred to me* to look for a plug-in solution.

But the biggest drawback to hourly billing is this:

Hourly billing places an artificial limit on your income.

There are only so many hours in the year, and you can only charge so much per hour, right? Let's say you wanted to double your hourly billing income. There are really only three ways to do this, and they're all pretty bad:

1. Work twice as much
2. Double your hourly rate
3. Hire a bunch of junior employees

I'll break down each…

1. Work twice as much

Working twice as much is obviously not going to be attractive to anyone. You probably feel like you're working too much already. In any case, it's unsustainable and doesn't scale your business in a meaningful way. Working more will decrease your productivity (and therefore produce diminishing returns) and eventually lead to burnout.

2. Double your hourly rate

Increasing your rate significantly will make it tough to close deals because the new rate will appear unfair or offensive in comparison to the old rate or market rate for similar services.

Existing clients - Significantly increasing your rate will be unattractive to your existing clients because you have conditioned them to believe that you are worth $X per hour. If you suddenly announce that you now cost $2X per hour, they'll likely consider this an unfair increase and start shopping around.

Prospective clients - Assuming that your rate is more or less in line with other folks in your industry, doubling your rate will make you the premium option. If you don't have anything significant that differentiates you from your competitors, you are not going to close many deals.

3. Hire a bunch of junior employees

Hiring juniors is probably the most seductive of the three growth options so I want to take a second to dispel any fantasies that might be floating around out there. If you hire junior employees, you will no longer spend your days doing the thing that you love; you will become a manager.

You will be posting jobs, reviewing résumés, writing training docs, managing benefits, sending tax documents, doing one-on-ones, boosting morale, demanding time sheets, generating productivity reports, and more.

Additionally, you will be responsible for client-facing administrative duties like writing proposals, closing deals, managing resources, tracking timelines, sending invoices, chasing late payments, haggling over hours entries, etc.

And let's not forget marketing and sales. If you have even a half-dozen employees, you're going to need a steady stream of leads to cover payroll every month. Every. Single. Month.

Sure, you *can* build a big profitable firm by hiring a bunch of junior employees. And if that's the lifestyle you want, then great! But if you don't want that lifestyle and are only considering it because you think it's your only option for growing your business, I'm here to tell you that there is an alternative: value pricing.

Introduction to Value Pricing

It is not the primary goal of this book to teach you about value pricing; the primary goal of this book is to shatter the illusion of hourly billing. That said, I have found that presenting an attractive alternative to hourly billing can be quite persuasive. Value pricing is that attractive alternative.

So let's talk about value pricing.

Value Pricing is like fixed bids on steroids. Unlike typical fixed bid quotes - which are based on cost-plus or time and materials calculations - the prices in a value priced quote are based on the client's perceived value of the project outcome.

But what exactly do I mean by value? I like this definition which I found from Ron Baker:

> Value is the maximum amount that a consumer would be willing to pay for an item

I find this to be an extremely elegant definition because it concisely illustrates the inherent subjectivity of value. Value is not an intrinsic property of an item - it's a vague sense of "what something is worth" to a particular person in a particular situation.

Many people are uncomfortable with the fluid nature of value but embracing this truth is the key to scaling your business in a sustainable way.

Fixed Bids? You've Gotta Be Kidding...

I can hear you thinking...

> "Wait a sec... are you talking about fixed bids?"

Yes, value pricing results in you providing a fixed price quote to your client.

And now I hear you screaming...

> "NOES!!! I'LL DIE OF SCOPE CREEP!"

No, not if you do it right you won't.

I've talked to a lot of consultants who have dabbled with fixed bids and gotten burned. In every case, they had based their fee on time and materials or cost-plus calculations. If you make this same mistake, then yes... you will probably get killed by scope creep because you'll set your fee way too low every time.

If you have been burned by fixed bids in the past, think back to the engagement and imagine how it would have gone differently if you had charged 2, 3, or maybe 4 times more money for it. I'm guessing you wouldn't have gotten killed. The secret sauce of value pricing is understanding why many clients are happy to pay more than double what you or your competitors are currently charging.

When you base your fixed price on the client's perceived value of the project outcome instead of your estimated labor, you can set your fees significantly higher, deliver more effective results, increase customer satisfaction, and more.

Shifting from billing clients by the hour in arrears to giving clients value-based fixed bids in advance is not as easy as flipping a light switch. For most people, hourly billing is baked into their business at every level (e.g., systems, culture, relationships, etc) and it takes time and effort to migrate away from it.

But migrating away from hourly billing is the key to unlocking profits that might seem unimaginable to you today. Keep at it. Like all worthwhile things, it takes a lot of effort but the payoff is huge.

> "Nothing in the world is worth doing unless it means effort, pain, difficulty." —Theodore Roosevelt

The Why Conversation

A value price represents some fraction of the amount that a prospective client thinks a given engagement will be worth to their business. For example, if a client thinks your project is worth $500,000 annually to them, then you can easily charge them $50,000 for the work, even if it's only going to take you a short time to complete.

But how do you figure out what something is worth to your client? You can't figure it out *exactly* (even they typically don't know exactly) but you can get close enough to drastically increase your fees. This is a gray area that folks are usually pretty uncomfortable with, but it's the key to closing highly profitable deals.

Here's how you do it:

Before you write up a project proposal, you'll have a meeting of some kind with your prospect. During that meeting, I'm going to have you do something unusual:

You're going to try to talk them out of working with you.

Yup. Just keep asking "Why?" until you are convinced that the client would benefit from hiring you. For example:

- "Why do this now? Wouldn't it be better to keep an eye on the issue for a few months?"
- "Why hire someone expensive like me? Couldn't you save a ton of money by outsourcing this to India?"
- "Why not use something off-the-shelf? Wouldn't that be cheaper than paying for custom code?"
- "Why even bother with what will clearly be a very expensive project? Wouldn't it be cheaper to do nothing?"
- "Why pay me to advise you on this for a year or more? Wouldn't handling it in-house deliver more long-term benefit?"

For obvious reasons, I call this the "Why Conversation". By the end of a good Why Conversation, you will have a pretty good idea of what the company's desired outcomes are, and roughly what those outcomes are worth to them.

To calculate your price, divide the value by 10 and ask yourself, "Would I do the project for this price?" If the answer is "hell, no!" then you probably aren't a good fit for the project and should politely refer the prospect to someone else. If the answer is "hell, ya!" then you have found your price. Write up the quote at 1/10 of the estimated value and send it to the prospect.

If your answer is somewhere in between, go back and divide the value by 5 instead of 10 - if you get a "hell, ya" then submit a quote, if not, refer them to someone else. Dividing by a number smaller than 5 is probably a waste of time because you're working with very rough numbers. Smaller divisors make it more likely that there won't be enough margin between the low end of the value range and the high end of the cost range for anyone to make a profit.

Three Ways To Transition Away From Hourly Billing

In my coaching program, I have found it is pretty hard for most students to transition straight from hourly billing to value pricing. The hourly mindset infects every aspect of most businesses so thoroughly and completely that it's impossible for the owner to imagine that there is an alternative. I have come up with the following three methods for easing into value pricing:

1. Add a fixed price option to an hourly proposal
2. Value price a small chunk of a larger hourly project
3. Create a productized service

(NOTE: Strictly speaking, these approaches are not value pricing. They are transitional steps that will help you break the habit of trading time for money. Once you do that, value pricing will appear relatively obvious.)

1. Add a value priced option to an hourly proposal

This is the easiest way to dip your feet in the water with value pricing. I quite like it because it makes evident the inherent lunacy of hiring someone by the hour to do software project work. It can also help with converting existing clients over from hourly billing to value pricing.

Here's what you do:

The next time you're ready to send an hourly estimate to a client, simply add a premium priced fixed price option.

The fixed bid should be roughly 85% more than the estimate

So, if your estimate is $10,000.00, then the most the fixed bid should be is $18,500.00.

If $18.5k for the fixed bid feels too low or too risky, then your estimate is too optimistic and you should increase it.

For example…

Let's say you are about to send your client a proposal for 100 hours of web development work at $100/hour. Make the $10,000.00 hourly estimate Option 1, and add a fixed price Option 2 where you guarantee results for $18,500.00 paid 100% up-front.

Doing so does a few things:

1. It will get everyone thinking about results instead of deliverables.
2. It will make the client explicitly aware of the fact that hourly billing doesn't guarantee results, just labor.
3. It will help you understand how to have a better value conversation next time.
4. You will increase your odds of closing the deal.
5. You will decrease your odds of leaving money on the table.

If you do have your two numbers within the 85% range and get push back from the client about the delta seeming extravagant, point out to them the difference in the risk profiles. Namely, that the estimate puts all the risk on them, and the fixed price puts all the risk on you. If they are open to rolling the dice with the lower number, that's up to them.

2. Value price a small chunk of a larger hourly project

Another way to get started with value pricing is to break off a small chunk of a larger project and quote a fixed price for it. I've done this on occasion with new builds where the client wasn't 100% clear on what they wanted.

In a situation like this, you can try charging a flat $1000-$5000 for a roadmapping phase that will result in a clear definition of what should be built. It's like helping the customer author the RFP that they aren't expert enough to author themselves. The output of this would be some combination of reports, documentation, wireframes, prototypes, style guides, user journeys, business logic, and so on.

To decrease the odds that the customer will balk at paying for discovery that they feel you should be doing as part of the larger project, you should emphasize that the roadmap is completely portable with zero lock-in. In other words they don't have to hire you to execute the plan - they can shop it around to any firm to do the actual build.

3. Create a productized service

A productized service is a lot like a custom service except that you don't write a proposal for it; instead, you write a sales page for it. In fact, sometimes the easiest way to spin up a productized service is to go back through your custom proposals and convert one into a sales page. Good candidates for productized services are activities that tap your smarts rather than your labor. This will make them more naturally limited in scope.

Here's an example:

I'm recognized as an authority on responsive web design. Building custom responsive websites from scratch would be very hard to productize because client demands would vary greatly from project to project (I could solve this by setting the price astronomically high, but that's a separate conversation).

However, I can think of a few services that would leverage my expertise and authority in the space without inviting a scope nightmare. I could offer a service where I will tweak your existing desktop site such that it will pass Google's new mobile SEO ranking criteria. Or I could offer a site teardown that was delivered as a report detailing the 10 worst mobile issues on your site, and the things that you could have your developer do to fix them.

The trick here is to think of new ways to leverage your expertise. Are you a JavaScript developer with ten years of experience? Instead of coding for clients, why not offer a service that helps your client pick the best front-end framework for their needs? Or front-end performance reviews? Or a "de-jank" consultation?

You want to charge for your head, not your hands. Smarts, not labor. Results, not deliverables. Outcomes, not activities.

Think about it.

Value Pricing FAQ

Recently, I was having an initial kickoff call with a new coaching client. We were planning to work on a number of issues, but his primary interest was converting his consulting business from an hourly billing model to a value pricing model. As with most folks new to value pricing, he had some practical questions about the approach. Several common points were raised, which I have shared below.

Fallout From Bad Estimates

You can underestimate just as easily with value pricing project as you can with an hourly billing project. The difference is the fallout. Specifically, if I underestimate an hourly project, my punishment is angry phone calls, endless review of hours entries, running reports and billing statements… IOW, a bunch of administrative BS and fights with the customer.

On the other hand, if I underestimate a value priced project, my punishment is… more development work. Guess what? I love development work. That's why I do this job. Sure my profit margin is decreased, but doesn't making $100/hr instead of $200/hr sound a lot better than arguing with a customer for an hour over a 30 minute timesheet entry?

Value Pricing Feels Different

To really understand the difference between value pricing and hourly billing, I think you need to do at least one project yourself. You need to feel the internal shift - the loss of the safety net, the spike in efficiency, and the changes in behavior that these feelings encourage. This shift will make you a better developer, advisor, and partner.

Converting Existing Customers

You don't have to convert to value based all at once. And, it's HARD to convert existing customers. Try it on a single project with a new customer first. Trying to re-frame all of your experience from a value based perspective ("how would I have done all these deals with value pricing") before internalizing the approach is a recipe for failure.

Cost vs Value

There are two numbers that you need to determine when bidding a project: the cost to you and the value to them. So, when I talk to a client about a new project, I first guess at how many hours I think it will take me, and I multiply that by $200 to come up with X. Then, I guess how much it is worth to the client and I divide that by 10 to come up with Y. I then give the client a quote for the greater of X and Y.

Success with this approach is clearly dependent on the accuracy of the guesses, but if Y is significantly greater than X - say, five or ten times greater - then the risk is drastically reduced. The closer Y is to X, the more sure you want to be of your guesses.

Fixed Bid vs Value Pricing

There is a difference between a traditional fixed bid and value priced quote. Ultimately, both result in a static priced quote to the client, but fixed is based on a cost estimate to the developer and value is based on a percentage of the value to the client. Hence, fixed bids are almost always too low.

Favorable Payment Terms

Payment terms are intrinsically related to the way I practice value pricing. You could do value-based projects and take payment in installments, or in arrears, but I recommend against it. Rather, submit your quote with the most favorable terms (i.e., 100% up front). If the client balks - although I find that most don't - it'll give you something to concede in negotiations.

Exceptions to Value Pricing

You can't use value pricing for everything. Value pricing is primarily for writing a custom proposal for a particular client. Products and productized services, for example, are *bought* on value but the prices are not *set* on value. They are a volume play meant to be profitable at scale. Think of it like this: if you're in a situation where you're tempted to present an hourly estimate to a client, consider using value pricing instead.

100% Up-Front

One of the wonderful side benefits of ditching hourly billing for value pricing is that you can ask for 100% payment up-front. This sounds pretty unorthodox to most people and I've gotten a bunch of questions about it. Here are the three most common:

- Why I ask for 100% up-front payment
- How often I "get away with it"
- What I do when clients push back

I'm going to answer all of those questions here but before I do, you need to know something very important:

I NEVER lower my prices once I have submitted a proposal.

Seriously. Never, ever.

Since I refuse to budge on price, I need to give myself room to negotiate in other areas. This is where my payment terms come in. Here's a typical example of the payment terms I offer:

> TERMS AND CONDITIONS
>
> I never assess an hourly or daily fee, since you should not have to make an investment decision every time my assistance

> may be needed. This is a unique feature of my consulting practice.
>
> The pricing for each option is as follows: option 1 is $4,900.00, option 2 is $9,500.00, and option 3 is $24,000.00 USD. Please note that these are fixed prices, not estimates. You will not pay a dime more than your selected price. The fee must be paid in full on acceptance to schedule the project. I am available to start on Monday, May 11, 2015. This quote is good for 30 days.
>
> My work is guaranteed. In the event that you feel that I am not meeting the standards described herein, or based on our mutual conversations and agreements, I will refund your entire fee upon such notification.

Roughly 80% of the time, clients agree to these payment terms without question. In the 20% of cases where a client doesn't, their reply is usually one of the following:

1. "Are you CRAZY?!" (aka Sticker Shock)
2. "How about 50% now and 50% on completion?" (aka 50/50 Terms)

Sticker Shock

In the "Are you CRAZY?!" scenario, my prices were just way too high and the prospect is suffering from an acute case of sticker shock. It's almost impossible to revive the deal at this point so I usually just thank them for their time and move on. (In the rare case when I really want the client, I have a backup approach that can sometimes revive the deal but that's a story for another day...)

50/50 Terms

In the "How about 50% now and 50% on completion?" scenario, my prices are in the ballpark but I haven't built up quite enough trust with the client. To mitigate their perceived risk, the client offers 50/50 payment terms - i.e., "How about we do 50% up-front, 50% when the work is done?"

My reply to them looks like this:

> We can discuss but I don't think it is in your best interest. A software project is like a lake freezing - at some point you are sure it's solid, but you never know exactly when it happened :-)
>
> In other words, we are not going to know exactly when this project is done. Tying the final payment to the delivery date will put pressure on you to sign-off too soon.
>
> If some bug crops up in a weird corner case three months after your sign-off, I'd prefer to just fix it for free under the terms of this agreement (vs what most other consultants would do: "Sorry, you signed off. I'll fix it but it's going to cost you.")
>
> To remove the sign-off issue, what would you think about doing 50% to get started and 50% in 30 days?

Almost every prospect to whom I've suggested this alternative has accepted. Once or twice, I've had a prospect balk at my suggested date (i.e., 30 day from project start), to which I say:

> That's fine. The exact date doesn't matter to me. Pick whatever date you think is reasonable and we can get started.

In this case, the client will probably pick a date around when they think the project will be completed. This date will almost surely be too early, but having agreed to a specific fixed date for the final payment allows everyone to relax about the sign-off (because there won't be a sign-off).

A wonderful side effect of this agreement is that if the client goes dark, you won't really care because it doesn't delay your final payment. They can take all the time in the world to respond to requests for feedback, provide copy changes, send FTP info, etc… It won't matter to you because you'll still get paid in full on a known schedule and can do other work while you wait for them to get back to you. No pressure for you, no pressure for them.

Win Win

Ultimately, asking for 100% up-front is better for you, better for the client, and better for the project. Give it a shot on your next proposal - you'll be pleasantly surprised by the results.

Managing Multiple Projects Without Deadlines

I have a policy of not agreeing to deadlines for software projects. I've received a bunch of questions about this. Here's a typical one:

> I am curious how you balance projects like you do without an end date. In the scenario you paint with 100% up front but client takes too long at the start of the project to get things started so the project doesn't wrap up on time. You have signed another client or two which starts after you initially thought the first project would wrap up because you need more income. Now the first client you signed is starting to really ramp up but you have two more clients to juggle. How do you handle this scenario?

I have two answers to this question - the short one and the long one.

The Short Answer

Deadlines don't keep projects on track - diligent communication keeps projects on track.

If you need Client A's Project to wrap up on or around a particular date so you can get started on Client B's Project, then it's up to you to manage Client A. Setting an arbitrary deadline won't help with this. If you find that you just can't manage Client A, then you should consider firing them (or at least not working with them in the future).

The Long Answer

You probably shouldn't be scheduling software projects back-to-back in the first place.

Scheduling projects back-to-back can be an indication that your margins are too tight, or that you're trying to "make hay while the sun shines" (i.e., you're in the "feast" phase of the feast/famine cycle), or that your business is not diversified enough.

In my particular case, diversification has shielded me from project scheduling issues. I virtually never schedule software projects back-to-back. I just don't need to because I maintain a balance of money making activities. Each has a very different profile in terms of how much effort they require, when that effort is required, and whether I can pick it up or put it down without significant switching costs.

Here are some examples:

- Monthly retainers (i.e., clients pay a flat monthly rate for 24/7 access to pick my brain)

- Speaking engagements (e.g., public conferences, corporate events, board presentations)
- Training classes and workshops
- Miscellaneous dev work (e.g., code reviews, teardowns, prototypes, proofs of concept, feasibility research)
- Book and video sales

All of these offerings have pros and cons, but there are a few that are worth highlighting.

Monthly retainers have been the big winner for me. They are very stable, low risk, and much more lucrative than dev work. I can run two or three of them concurrently and they pay five figures monthly. I've had a number of retainer clients keep me on for a year or more.

Speaking engagements are very good money but you're not going to be doing them every day; I shoot for roughly one per month. I've gotten as much as $7500 for a 1-hour speaking engagement, but my average is probably closer to $4000. Added bonus: speaking gigs are great for positioning yourself as an authority and often lead to high-value engagements like retainers or other consultative work.

Training classes and workshops have been similar in frequency and fees to speaking engagements for me, but they are more work to set up and deliver. If you're currently just doing dev work and want to branch out without too much risk or fear, then training classes and workshops are a great place to start.

Diversification FTW!

This mix of offerings has been so strong for me that these days I rarely code for money. It's just not worth the time, risk, or stress. Instead, I keep my dev skills sharp by working on side projects or creating educational materials. And every once in a while I'll make an exception and take on a client project that I find particularly interesting or meaningful (but this usually only happens once or twice per year).

If you're booking projects back-to-back, try to think of ways you can sidestep the issue by offering a wider range of services.

One path that should work for most devs would be to start with training classes or workshops, move into speaking engagements, and ultimately to monthly retainers. Along the way you can release info products (e.g., books, videos) and pickup one-off miscellaneous work (e.g., code reviews, teardowns, prototypes, etc).

How To Prevent Scope Creep

When I talk to a roomful of software consultants about transitioning away from hourly billing to value pricing, one of the first questions I get asked is:

"How do you prevent scope creep if you give clients a fixed price?"

My answer is simple:

"I don't."

The truth is, I don't have to. I trust my clients to not take advantage of me. And guess what? They don't take advantage of me.

The Baseball Bat

Consultants use hourly billing as a baseball bat. When the client asks for something that's out of scope, the consultant hits the client with the bat. Statements like these probably sound familiar:

"That feature was not part of the original estimate. I'll build it for you, but it's going to cost you."

"I'd be happy to discuss that with you, but it'll have to be on the clock."

"You should have told me about that earlier. This is going to blow the estimate."

When a consultant says that he has to bill by the hour in order to prevent his clients from abusing his time, it tells me that he doesn't trust his clients. Which raises a key question:

Is it reasonable to expect people to trust you if you don't trust them back?

True Story

Back when I worked hourly, I had this one client who was really chatty on the phone. He'd tell me about his weekend, his kids, etc. I genuinely liked the guy, and we'd often spend 30 minutes or so gloriously gabbing about life, liberty, and the pursuit of happiness.

Unfortunately, this non-work banter created an issue for me. My employer was billing me out by the hour and I was responsible to have a certain number of billable hours per week. So, for every 30 minutes of shooting the breeze with my client, I had to work an 30 extra minutes in the day in order to meet my quota.

I explained this predicament to my client on several occasions. I'd say something like: "I'd love to hear about how you proposed to your wife, but I have to get back to work." Of course, he would say he understood and things would be strictly business for a little while. But soon enough, he'd start gabbing again.

Eventually, I pulled out the bat. I started tracking the time spent on the phone - regardless of the subject matter - and billed him for it. I'm sure you can imagine the effect this had on our relationship.

The Moral

When I think back on this situation, I just shake my head. Consultants should jump for joy if clients are willing to share personal details of their lives! It builds trust, which is an essential ingredient to a successful relationship, business or otherwise. Throwing this opportunity away because of 30 "lost" minutes here or there is asinine.

If you are a consultant, value pricing will allow you to build trusting relationships with your clients. This will lead to more successful projects, repeat business, and in many cases, rewarding friendships. However, it does require that you put down the bat.

Useful Estimates

I recently did a proposal tear-down for a coaching student (I'll call him Chris). The proposal was for a client who has three silo'd software systems and Chris was proposing to consolidate everything into one system to alleviate a lot of inefficiency and frustration.

The proposal was pretty good overall, but there was one paragraph that really rubbed me the wrong way. Here's what Chris wrote:

> The benefit from the system is not easy to substantiate financially. The savings of personnel time and the simplification of the computing infrastructure, although they will have long-term financial effect, cannot easily be measured. Instead, this is an investment of strategic importance.

Ouch. Just at the point where Chris should have been quantifying the value of the project to the client, he threw up his hands and said, "I have no idea how much money this project will save your business!"

Here's the thing:

Just because something is hard to measure, doesn't mean that you can't make a useful estimate.

I suggested he change the paragraph to something like this:

> Although it is hard to say *exactly* how much financial benefit the new system will provide, estimates can be made. We predict that the new software will save each user at least 1-2 hours of work per week. If you multiply that by 10 users making roughly $20/hr, and again by 50 working weeks per year, the software will save between $10k-$20k annually.

Naturally, Chris would be spit-balling the numbers somewhat, but the client can easily adjust up or down in his or her head. In any event, $10k-$20k is way better than "I have no idea how much you'll save." Having numbers–even estimated numbers–gives you something to anchor your price against, which makes it much easier to get your proposals approved.

P.S. There's another angle to this situation that bears mention. Namely, that Chris should not have had to estimate the financial benefits at all. Instead, he should have had a conversation with the client before the proposal stage, during which he helped the client articulate what the project would likely be worth to the company.

11 Questions To Ask Clients Before Writing Your Proposal

When I used to bill by the hour, my initial conversation with a prospect was all about determining the scope of work so I could come up with what I hoped would be a reasonably accurate cost estimate. Now that I price based on value, I don't bring up scope at all in my initial conversation. Instead, I try to find out how valuable the project is to the client so I can decide if there's any hope of me delivering positive ROI. This can be a simple thing to do if you know what to ask, are a good listener, and take good notes.

When you meet with a client, work some of the following questions into the conversation as appropriate. You don't need to ask them all—pick three or four that you're comfortable with and memorize them. Modify the wording to suit your style so you don't feel awkward saying them out loud.

Once you have their answers, you'll be ready to create a proposal that uses the client's language and is priced based on the value they themselves have expressed. This greatly increases the likelihood that the client will greenlight your project.

Without further ado, the questions:

1. What would a home run look like for you?
2. What about your business keeps you up at night?

3. If you could wave a magic wand and change one thing about your business, what would it be?
4. What's been at the top of your to-do list forever?
5. Is there anything that your competitors could do that would threaten your business?
6. How do you acquire new customers?
7. Have you been putting off any difficult decisions?
8. Does your business go through slow periods (weekly, monthly, yearly)?
9. If you had to set priorities now, what three things must be accomplished?
10. How has your business performed over the last 12 months?
11. Is there anyone on your team who isn't performing up to your expectations?

How to make $2000+ “per hour”

If you’re like most folks, you probably think that “growing your business” is synonymous with “hiring employees”. I’m living proof that hiring is not the only way to grow your business. Hiring more laborers is multiplying your hands. The real growth comes from figuring out how to multiply your head. But how do you multiply your head?

Like so:

- Solving bigger problems
- …for bigger clients
- …with less effort.

If you are always looking for bigger problems, and attracting bigger clients, and decreasing your own labor, you can exponentially increase the impact of your smarts - and as a side effect, drastically increase your effective hourly rate (EHR).

Here’s an example:

I’m writing this to you from a fancy hotel room in southern California. It’s gorgeous outside. My balcony overlooks a golf course on one side and a marina on the other. Somebody is literally yelling “FORE!” as I type this.

I'm here to present a talk to a group of about forty senior managers and executives. My talk is grounded in technical topics that I learned in my career as a developer. BUT I'm presenting it in a way that is meaningful to business leaders.

The talk is one hour long. I got paid $6,500.00 USD for this, 100% in advance.

It wouldn't be fair to say that the talk REALLY only took me one hour - I had to fly cross country, for example - but when you consider my level of effort, my level of risk, and my time commitment, I think you'll agree that my EHR is pretty dang good.

And OBTW, I'm giving the same talk again in two weeks to a different group.

And again, two weeks after that.

Now, I'm not saying that you should start trying to sell yourself as a speaker if that's not your thing. What I am saying is that you should be looking for ways to increase your impact without increasing your workload - and especially without increasing your headcount.

An ‘A’ For Effort?

Which of the following criteria should be used to calculate a student’s exam grade?

1. Amount of time spent working on the test
2. The percentage of correct answers

Which of the following criteria should be used to calculate a consultant’s fee?

1. Amount of time spent working on the solution
2. The progress made toward the client’s goals

Moral of the story:

Clients don’t want your time; they want their goals achieved.

In fact, the faster you achieve their goals, they more they’ll be willing to pay!

Hourly billing is nuts.

Cost is not Price is not Value

When discussing value pricing, three words come up all the time:

- Cost
- Price
- Value

Lot of folks use these words interchangeably which leads to confusion. For the purposes of my coaching, it's important to be crystal clear on these terms, which I define thusly:

Cost - The least amount of money a seller (i.e., you) will accept for a product or service.

Price - The amount of money exchanged between buyer and seller.

Value - The largest amount of money a buyer (i.e., your client) will pay for a product or service.

When value pricing is working well, your cost is less than the price, and the price is less than your client's value.

Let's imagine a small web dev project that might have numbers like this:

Cost: $1,500

Price: $2,000

Value: $3,000

The difference between cost and price (i.e., $500) is your profit. The difference between price and value (i.e., $1,000) is your client's profit. This is the ideal scenario because both parties make a profit from the engagement.

(BTW - this is why clients freak out when hourly jobs go over estimate; because the price starts to approach or exceed their value).

As you get better at value pricing, you will dream up offerings that have lower cost and higher value.

For example, imagine presenting a remote workshop that provides 10x profit for both parties:

Cost: $1,000

Price: $10,000

Value: $100,000

Or let's say you offer a cloud computing optimization report that provides 20x profit for both parties:

Cost: $50

Price: $1,000

Value: $20,000

Numbers like these give you much more wiggle room AND higher profit for both parties AND less work for you AND often faster delivery for the client. Monster win!

Revenue vs Profit

As software developers, we tend to discount our time.

And by “discount” I mean “forget about”

Let’s talk about revenue vs profit real quick…

Revenue — the amount of money you receive from your clients.

Profit — your revenue minus your cost.

Mkay, but what is the “cost” in this case?

If you’re a typical lone-wolf software developer, your costs might seem insubstantial:

- A laptop
- An internet connection
- Copious amounts of coffee

That’s about it right?

Wrong.

You forgot your biggest expense: YOUR TIME!

Think of it like this:

What if you continued to do all the biz dev, marketing, sales, admin, and project management, but PAID SOMEONE ELSE to do your dev work?

Even if your dev was the most amazing ever, and there was no communication latency, and nothing was lost in translation, this dev would certainly be your biggest project expense.

In other words, YOUR DEV WOULD EAT ALMOST ALL OF YOUR PROFITS!

(sorry for all the caps)

Now…

When you are chief, cook, and bottle washer, you tend to forget about counting your dev time as a COST.

But that's EXACTLY what it is.

I don't care how much you love coding… every hour you spend doing dev for a client, you are NOT spending an hour:

- Building tools to make your job easier
- Marketing your business
- Creating new products
- Contributing to open source
- Playing Unreal Tournament with me :)
- Hanging out with your friends
- Having cocktails with your spouse
- Playing with your kids
- Writing your memoirs

- Finger knitting (yes, it's a thing)
- etc…

Here's the money quote:

Development work is GREAT for revenue, but SUCKS for profitability.

Revenue is a vanity metric. What you want is profitability.

More Revenue != Growth

I was talking to a dev friend the other day who was proudly reporting his business “growth.”

The conversation went like this:

dev: “I hired 2 devs at the beginning of the year and I’m on track to double revenue!”

me: “That’s great but… you probably doubled your costs, right?”

…long pause…

dev: “Yeah, I guess you’re right.”

Remember:

Increasing your headcount is not growth.

Increasing your revenue is not growth.

Increasing your profits is growth.

Why Startups Are A Bad Fit For Value Pricing

Value pricing is virtually impossible if you can't talk to the true stakeholder.

This makes venture backed startups a really unattractive target market for value pricing.

Here's why:

Even if you're talking to the CEO, he or she typically still has to answer to partners and investors in order to make a final decision.

Furthermore, if the startup doesn't yet have a predictable revenue stream, it's very difficult to come up with a realistic value for whatever it is you might be doing for them.

In other words, the value can range from $0 to billions of dollars, depending on what happens in the future. So it's virtually impossible to calculate a fair price.

(It's like selling value-based services to a gambler - if he hits, the value ends up being huge; if he doesn't hit, the value is zero.)

There are some exceptions, but in general my advice to students is to avoid picking venture backed startups as a target market.

Two exceptions:

- Bootstrapped startups are fine because you can talk to the decision-maker
- Creating productized services for venture backed startups is fine (since productized services have a published price, buyers can self-select based on the value that they think they'll derive)

The Choice Is Yours

Hourly billing has always been a bad fit for pricing professional services but newer trends like globalization, offshoring, and spec work marketplaces have made this situation dramatically worse.

At a tactical level, it may be relatively hard for you to ditch hourly billing. But tactical challenges don't amount to much compared to the big picture. When all is said and done, the options at a strategic level are pretty straight forward:

Embrace hourly billing and race to the bottom, or reject hourly billing and race to the top.

The choice is yours.

Appendix I: More Info

Here's a TON of valuable free resources I've put together for you:

Webcasts

- How To Increase Your Income Without Hiring Junior Developers
- How To Price Your Services Without Leaving Money On The Table
- How To Write Proposals That Close Without Lowering Your Prices
- How To Prevent Scope Creep Without Writing Massive Spec Documents

Podcasts

- Elusive Moose Podcast: Value Pricing with Jonathan Stark
- Clients From Hell: When (And Why) You Should Stop Charging an Hourly Rate
- Side Hustle Nation: How to Start a Consulting Business - Your First $5k
- The First Million Podcast: Go from $0 to $5000 a month consulting with Jonathan Stark
- Boagworld: Break the time barrier with value based pricing

- Freelancers Show: How to Attract Clients Without Doing Sales with Jonathan Stark
- Freelancers Show: How and Why to Ditch Hourly Billing with Jonathan Stark
- The Business of Freelancing: Jonathan Stark on Risk Mitigation through Fixed Bid Pricing
- Consulting Pipeline Podcast: Jonathan Stark on the Paradox of Choice
- Art of Value: Do Not Assume in a Value Conversation with Jonathan Stark
- Pricing Power: Positioning eliminates the billable hour with Jonathan Stark
- High-Income Business Writing: Three Simple Ways to Transition to a Value Pricing Model
- FileMakerTalk: Jonathan Stark on Value Based Billing

Articles

- 100% Up-Front
- How I Realized that Hourly Billing is Nuts
- The Moral Dilemma of Hourly Billing
- How Hourly Billing Hurts Software Projects
- How To Prevent Scope Creep
- Hourly Billing Prevents Growth
- 7 Thoughts on Value Pricing for Software Projects
- The Benefits of Pigeonholing

Mailing List

Please sign up for my mailing list to receive proposal templates, email samples, and practical articles that will help you grow your business without adding employees.

Get my 5-page proposal template and more…

Questions?

Any questions? Shoot me an email at jstark@jonathanstark.com and I'll get back to you as soon as I can. Pro tip: the shorter your email is, the faster I'll be able to get back to you.

P.S. Need personalized actionable advice on growing your software development business? I'm available for a limited number of roadmapping sessions each month, and would love to help. Book a session now.

Appendix II: Glossary

> “There is no greater impediment to the advancement of knowledge than the ambiguity of words.” –Thomas Reid

The following glossary is meant to be understood in the context of my coaching program and may not necessarily represent the global definition of these terms in the strictest sense.

Since this document is directed specifically at students, I have used the words “you” and “yours” for clarity in places where I felt the concepts might be too abstract. In virtually all cases, these pronouns can be considered synonymous with “seller” or “vendor...”

Answer Bomb

A value-packed post written in answer to a question posed by someone in a Watering Hole. The goals of an Answer Bomb are to increase your authority, attract prospects, and inspire trust with Buyers within your Target Market. Care must be taken to not appear spammy or self-serving.

Audience

The collection of all people whose attention you have (e.g., Facebook fans, Twitter followers, email subscribers, webinar attendees, etc).

Benefit

The positive outcome gained by the client from your product or service. See also: Return On Investment, Value.

Beta Service

A new service that you provide for free to a test client in exchange for feedback, pricing, and testimonials/case studies. See also: Testimonial.

Buyer

Synonymous with Client in the context of abstract pricing discussions (e.g., “Value minus price equals the buyer’s profit”). Synonymous with Economic Buyer in the context of sales and marketing discussions (e.g., “What conference do your buyers attend every year?”).

Call To Action

A request for someone to do something, typically associated with a button or a link on a web page or in an email message (e.g., "like my Facebook page", "join my mailing list", "schedule a call", "buy my book", etc).

Charm Pricing

The practice of using non-round numbers for pricing in an effort to make them seem smaller (e.g., $29.95 instead of $30.00). Probably works best for no- and low-touch offerings in the two- and three-figure range. Low four-figure prices can be okay depending on the context, but once you get to high-touch premium services in the five- or six-figure range, they're probably insulting to the buyer.

Client

A business or business person who pays you for products and/or services. Synonymous with Customer, sometimes synonymous with Buyer. See Sales Funnel for more info.

Cocktail Party Answer

A succinct and conversational version of your LFPS. The name comes from the common scenario of someone at a cocktail party asking, “So, what do you do?” See LFPS for more info.

Conceptual Agreement

The goal of a value conversation is to reach conceptual agreement, whereby you and your prospect come to an explicit and mutual understanding of the underlying motivation, desired outcome, and progress metrics for an engagement. I believe this term was coined by Alan Weiss.

Conversion

An executed call to action.

Cost

The least amount of money a seller will accept for a product or service.

CTA

See Call To Action.

Customer

See Client.

Decision Maker

Person who decides whether or not s/he wants to hire you. Preferably (but not necessarily) the same person as the economic buyer (e.g., the CMO could be the decision maker, but s/he needs to get budgetary approval from the CEO).

Deliverable

Typically a low-value, tactical activity or artifact self-prescribed by a client who believes it will reach some underlying goal. Deliverables emphasize your labor, not your smarts, and are therefore to be avoided because the are not very profitable.

Demographic Market

A market segment defined by personal attributes of an individual (e.g., soccer moms, Asian Americans, billionaire philanthropists, migraine sufferers, etc).

Demographic Specialization

Niching Down on a Demographic Market.

Desired Outcome

See Objective.

Diagnosis

Assessment of a business's situation and underlying goals. A diagnosis should be performed before prescribing a course of action. Professionals have a moral obligation to do a diagnosis prior to prescribing action. Failure to do so would be considered incompetent. See also Self-Diagnosis.

Discipline

Your craft, specialty, or job title (e.g., web designer, iOS developer, systems architect, etc).

Drip

Email marketing automation software. http://getdrip.com

Economic Buyer

Person who controls the money in the client organization. Preferably (but not necessarily) the same person as the decision maker (e.g., the CMO could be the decision maker, but s/he needs to get budgetary approval from the CEO).

Effective Hourly Rate

The dollar amount obtained by dividing a fixed bid price by the number of hours worked.

EHR

See Effective Hourly Rate.

Engagement

Can be used two ways: 1. as a synonym for a project or other collaboration between you and your client, or 2. as a measure of audience interaction (e.g., "my audience is much more engaged now that I'm spending more time on my Facebook page").

Expensive Problem

A painful issue that a business is aware of. Potentially the answer an owner would give to a question like, “What keeps you up at night?”

Fixed Bid

A pricing model in which the sellers (i.e., you) provide a single, specific price for an entire project. Typically, this price is based on the seller’s costs (e.g., time and materials). Compare to Hourly Billing and Value Pricing.

Fool-Proof Positioning Statement

See FPPS.

FPPS

Acronym for Fool-Proof Positioning Statement. A term coined by Dan Janal to refer to a two sentence message that tells people what a product or service is, how they will benefit from it, and how it is different than others. http://www.smartbiz.com/article/view/156/1/4

Funnel

See Sales Funnel.

Gatekeeper

Person who blocks your access to the Economic Buyer.

Generalist

A person who markets themselves as capable of doing many different types of work for many different types of clients (aka "Jack of all Trades"). Contrast with Specialist.

Growth

Increasing profits. It's important to point out that many things are mistaken for growth. For example: hiring more employees, increasing gross revenue, capturing more market share, etc. These are growth tactics, and may *lead* to growth, but could just as easily lead to decay. Here's a fitness analogy: regular weightlifting will probably lead to muscle growth *but it is not synonymous with muscle growth*. A number of factors could prevent weightlifting from resulting in muscle growth. When your bicep is bigger today than it was yesterday, that is growth.

High-Touch

A sales process or service delivery that requires a lot of direct attention from you (i.e., the seller). Typical with custom software development projects.

Home Page

The top-level page of your website hierarchy. Not necessarily a landing page or sales page, but could be.

Horizontal Specialization

Niching Down on a skill, tool, or platform that can be applied to a very broad range of client types. e.g., responsive web design, iOS development, MySQL administration.

Hourly Billing

The practice of charging clients by the hour for your services. In the context of a software project, the process typically goes like this: you provide the client with an estimate that includes your hourly rate and the number of hours you expect it to take to complete the work. The client approves the estimate and you begin working. You track your hours as you do the work and invoice the client in arrears on a periodic basis (e.g., weekly, bi-weekly, monthly). Compare to Fixed Bid and Value Pricing.

JFS

Acronym for "Just Fucking Ship" by Amy Hoy. https://unicornfree.com/

Landing Page

A standalone web page distinct from your main website that has been designed for a single focused objective. Your landing page should have no navigation or other distractions. This is to limit the options available to your visitors, helping to guide them toward your intended conversion goal.

Laser-Focused Positioning Statement

FPPS as applied to a professional services business to position the business in a extremely specific way. It is typically not used verbatim in marketing materials, but rather as a guidepost for crafting various types of messaging (e.g., tagline, slogan, cocktail party answer, etc).

Lead

Person who is in your Target Market but has not been qualified yet as a Prospect. See also: Sales Funnel.

Lead Magnet

Something you offer for free in an effort to persuade people to subscribe to your mailing list. Typical examples are whitepapers, reports, cheatsheets, email courses, and so on.

Leverage

An effort multiplier. For example, a pre-recorded video course has more leverage than a custom development project because the effort it took to create the course will continue to generate sales income in the future with no additional effort, whereas the custom project work only pays once.

LFPS

Acronym for Laser-Focused Positioning Statement.

LOE

Acronym for Level Of Effort.

Low-Touch

A sales process or service delivery that requires little direct attention from you (i.e., the seller). Typical with productized services.

Marketing

Things you do to make people in your target market aware of your products and services (e.g., guest blogging, appearing on podcasts, speaking at conferences, etc). The goal of marketing is to create leads. See also: Lead, Prospect, Sales, and Sales Funnel.

Mats

Slang for materials (e.g., “I have to finish my mats for the webinar tomorrow”).

Nar

Slang for webinar (e.g., “I have to finish my slides for the nar tomorrow”).

Mercedes Option

Slang term for your most premium offering. Typically your highest price, highest profit, highest touch, custom service.

Niche

A specialized but profitable corner of the market.

Niching Down

Moving from a generalist position (e.g., full-stack web developer) to a more specialized position (e.g., Shopify consultant).

No-Touch

A sales process and product delivery that requires no direct attention from you (i.e., the seller). Typical with info products.

Objective

A desired outcome. For example, “Destroy the Death Star.” See also: Strategy, Tactics.

Offering

Something you sell (i.e., a product or service).

Perceived Value

See Value.

Pigeonholing Yourself

See Niching Down.

Pipeline

Scheduled work (e.g., "my pipeline is full through the end of this year").

Platform Specialization

A subset of Horizontal Specialization that targets a tool or platform that *your ideal buyer* was involved in choosing. Niching Down on Shopify, WordPress, or Salesforce are examples of Platform Specializations because your buyer almost certainly was involved in choosing the technology in question. Niching Down on tools like Photoshop, JavaScript, or MySQL are not Platform Specializations because they buyer probably didn't directly or consciously choose them.

Positioning

A marketing technique used to make your business more memorable. For service providers, this is done by focusing your marketing message on a particular facet of your business, on a specific target market, or both.

Preso

Slang for Presentation. A lecture-style event delivered live in person (e.g., conference session, workshop, keynote presentation) or over the internet (e.g., webinar). A recording of such event may be referred to as a preso for short, but really it is a recording of a preso - e.g., "Here's a link to (a recording of) my preso at SXSW.."

Price

The amount of money exchanged between Buyer and Seller. A price is typically known to the buyer in advance of making his or her purchase decision. A notable exception to this is hourly billing wherein the buyer makes the purchase decision on the basis of an estimate.

Product Ladder

A series of offerings priced in a graduated "order of magnitude" fashion (e.g., $10, $100, $1,000, $10,000). The idea of the product ladder is to make it easy to turn prospects into customers regardless of the level of trust you have engendered with them. In other words, people who have just heard of you will most likely enter at the bottom rung of your ladder (e.g., $10). Assuming that they benefit from that purchase, they will have increased trust and be more likely to move up the ladder.

Productized Service

A high-touch, customized service that you offer at a published price. Basically the same as a custom service except that you don't have to write a proposal for it, and it will have a fairly fixed scope.

Project

A collaborative enterprise that is designed to achieve a particular aim.

Prospect

Person who is likely to buy from you but has not done so yet. See Sales Funnel for more info.

RFP

Stands for Request For Proposal. Also known as Request For Quote, Bids, and Tenders.

Roadmap

A plan for getting from current state to desired state.

Retainer

A specific type of productized service where you offer your clients access to your expertise on a subscription basis - typically monthly but sometimes quarterly or even annually. A client asks you a question over an agreed upon channel (e.g., phone, email, Basecamp, Slack, etc) and you answer within an agreed upon time frame (e.g., "within 90 minutes for requests made during business hours, next business day for after hours requests"). Think of it as a hotline to your brain. NOTE: Not to be confused with a typical legal retainer, which is really just pre-payment for blocks of hours.

Return On Investment

The client's profit, typically measured in financial terms. Calculated by subtracting the price paid for a product or service from the value of the outcome. Ideally, ROI is positive but can be negative. Positive ROI can be thought of as a benefit.

ROI

See Return On Investment.

Rolodex Moment

A Rolodex Moment (RM) has occurred when someone you're talking to is inspired to mentally run through the list of people they know and successfully comes up with one or more who they should introduce you to for business reasons. This will typically be in response to the listener's first exposure to your CPA or LFPS. RMs are most likely to occur in your audience if you have adopted a Vertical Specialization or a Demographic Specialization (e.g., "I help dentists" or "I help people who suffer from migraines"). RMs are unlikely to occur in your audience if you have adopted a Horizontal Specialization (e.g., "I help people who need QuickBooks integration").

Sales

The things you do to convert a lead into a prospect, and hopefully into a client. See also Sales Funnel.

Sales Funnel

A system or process for turning a Lead into a Client. For custom software projects, this process would look something like:

1. Receive a Lead via email
2. Have a Value Conversation
3. Reach Conceptual Agreement
4. Lead is now a Prospect
5. Submit a Project Proposal
6. Prospect approves the Project Proposal
7. Prospect is now a Client

Sales Page

A specific type of Landing Page where the conversion goal is to persuade the visitor to make a purchase. See Landing Page for more info.

Self Diagnosis

Clients often come to consultants with a self-prescribed course of action based on an unstated self diagnosis. It is the responsibility of the consultant to validate the client's desired course of action prior to any engagement. Doing otherwise would be unethical and is grounds for losing the right to practice in other professions (e.g., medical, legal).

Slogan

See Tagline.

Social Proof

Endorsements (tacit or otherwise) of your work from third parties. For example: testimonials, case studies, client lists, etc.

Specialist

Someone who markets themselves as having a sharply focused area of expertise. The area of expertise is typically defined by the overlap of the specialist's Discipline and the needs of the specialist's Target Market.

Squeeze Page

A specific type of Landing Page where the conversion goal is to persuade the visitor to subscribe to a mailing list. See Landing Page for more info.

Strategy

A concise, high-level approach for reaching an objective using various tactics. For example: “Take the Empire off guard by sending an absurdly small force to exploit a critical vulnerability.”

Street Cred

Evidence of expertise. Some kind of irrefutable proof that you know what you’re talking about. The more impressive the evidence, the more credible your claims of expertise. The better your street cred, the easier it is to build trust with people in your target market. For example, Stephen King’s street cred as a writer would instantly make him trustworthy as a writing coach.

Tactics

Specific, individual steps used to execute a Strategy and reach an Objective. For example, “Send 3 small squadrons of x-wings. Get close to surface of the space station and head for the exhaust port. Stay deep in the approach trench to avoid surface guns. Once the TIE fighters show up, have two x-wings flank the leader and defend against enemy fire…”

Tagline

A memorable, succinct, and descriptive version of your LFPS for use in places like the title tag of your web page. It is typically expressed in written form, but could also be spoken in certain business contexts (e.g., as you're being introduced prior to being interviewed on a podcast or walking on-stage to present at a conference). Synonymous with slogan. See LFPS for more info.

Target Market

A specific group of people who you specialize in serving. Typically this group will be defined in terms of a vertical market (e.g., quick service restaurants, cosmetic dentistry, ski resorts), but could be a demographic (e.g., soccer moms, Asian Americans, billionaire philanthropists), or a horizontal technology (e.g., businesses who have mission critical dependencies on WordPress, Shopify, Heroku, etc). A rough test for determining the viability a potential target market is whether or not there is a conference that is attended by buyers from this group. See also Vertical Market, Demographic Market.

TBA

Acronym for "The Brain Audit" by Sean D'Souza. http://www.psychotactics.com/products/the-brain-audit-32-marketing-strategy-and-structure/

Teardown

Constructive criticism of a web page, email message, sales letter, or other marketing piece. A teardown can't be done properly without knowing the desired outcome of the marketing piece.

Testimonial

Kind words from a client about your product or service. Used in your marketing materials to build trust with members of your Target Market.

Testy

Slang for Testimonial.

TPM

Acronym for "The Positioning Manual" by Philip Morgan. https://philipmorganconsulting.com/authority-resource-center/the-positioning-manual-for-technical-firms/

Unique Difference

Component of a LFPS meant to make you stand out from your competition. Your primary differentiator.

Value

The largest amount of money a buyer would pay for a product or service. IOW - what a given product or service is worth to a given buyer. This is a purely subjective measure; different buyers will value the identical product or service differently. Furthermore, buyers will usually be unable to assign a dollar amount to a value if asked. However, they can usually react to a dollar amount suggested by the seller as “worth it” or “not worth it.”

Value Conversation

A meeting between you and a prospect held prior to submitting your project proposal. The goal of the meeting is uncover the underlying motivation, desired outcome, and progress metrics for a project. Achieving this goal means that you and your prospect have reached conceptual agreement.

Value Pricing

A form of Fixed Bid in which the price is based on the value to the buyer instead of the seller’s cost. Compare to Fixed Bid and Hourly Billing.

VBF

Acronym for “Value-Based Fees” by Alan Weiss. http://www.amazon.com/Value-Based-Fees-Charge-Youre-Worth/dp/0470275847

Vertical Market

A vertical market (or simply “vertical”) is a market in which vendors offer goods and services specific to an industry, trade, profession, or other group of customers with specialized needs. Typical examples of buyers in a vertical market would be quick service restaurants, ski resorts, pet shelters, auto repair shops, and so on. Technically, vertical market buyers could also be people like soccer moms, Asian Americans, billionaire philanthropists because these are also groups who have specialized needs. However, I prefer to use the term “demographic” to apply to segmentation that is not industry specific. See also: Target Market, Demographic Market.

Vertical Specialization

Niching Down on a Vertical Market.

Watering Hole

A place where Economic Buyers from your Target Market discuss business matters. Could be conferences, professional associations, meet-ups, industry periodicals, podcasts, Facebook groups, LinkedIn groups, subreddits, private forums, Amazon book reviews, and so on. Watering Holes are a great place to do market research and drop Answer Bombs.

WOM

Acronym for “word of mouth.”