

Pricing: Another Side to the Profit Equation

There's been a lot of talk about cost-cutting over the past few years as companies of all sizes strive to increase profits. When it comes to increasing profits, however, reducing costs is only part of the story.

"Companies will do everything in their power to cut costs, from outsourcing IT departments to limiting employee travel. But there's another side to the profitability equation that often goes unexplored – pricing," says Greg Peters, CEO of Zilliant. "Pricing is the last bastion of guesswork in American business, but research shows companies that make pricing a priority, and implement solutions from a specialized pricing vendor like Zilliant, can see a profit improvement, sometimes as high as 20 percent."

A survey conducted at the Pricing Institute's 18th Annual PriceX Conference held in Chicago, Illinois in June, found that:

- 61 percent of companies use a spreadsheet to determine price not a specialized pricing application or vendor
- 56 percent of companies have some sort of pricing strategy in place
- 44 percent of companies have a dedicated pricing person or department responsible for pricing
- 35 percent of companies consider pricing a top priority.

Reuters reports another survey, this one of members of the National Association for Business Economics (NABE), found that 38 percent of respondents reported higher prices during the second quarter. Additionally, 43 percent of respondents anticipated raising prices during the next three months.

Of course, pricing accounting services, as well as other professional services, is a little more challenging than pricing a product like a car, computer or even a shirt. Deciding whether to raise prices, and by how much, is even more challenging. Most services are priced using one of six common methods:

- **Strategic pricing** uses a pricing level low enough to lure clients or win bids away from competitors. It is intended for temporary or short-term use and assumes that once a client has experienced the service they will stay with it even if the price changes.
- **Parity pricing** reflects what other firms charge or are likely to charge. Often, they are tied to fee benchmark lists published by professional associations, business publications or industry groups.
- **Negotiated pricing** occurs when a client tries to negotiate the price of a service or the types of services covered by the price. Often this method is used in bidding situations or when the client maintains a list of preferred vendors who regularly compete to provide services.
- **Sociopolitical pricing** occurs when pricing is affected by the type of client, by client characteristics or by the type of work needed. This pricing is frequently considered "pro-bono" work or used to break in to a new area of practice.
- **Cost pricing** uses both the direct and indirect costs of providing the service then adds an amount for profit to determine pricing. This is the most popular pricing method among professional service providers and is commonly expressed as the billable charge per hour.
- **Value pricing** attempts to balance what clients think a service is worth with the costs of providing the service and the amount of profit desired. This method works best for firms with established and superior reputations.

Whichever pricing method is used, to be sure it is fair and reasonable professionals need to record all the tasks, equipment, staff and external charges (such as printing fees, long-distance phone calls or mileage for travel to client sites) associated with the service and the precise amount of time spent performing each needs to be recorded and audited on a regular basis. Indirect costs, especially overhead, should also be monitored regularly to ensure they do not increase unexpectedly. The level of profit or where the firm is in relation to its profit goal also need frequently progress checks. Understanding how prices are determined and using up-to-date data in the calculations allows individuals to respond with confidence to pricing inquiries beyond just quoting a figure. It is also an advantage over less self-aware competitors.

"Pricing is generally accepted as a core business practice, but the process some companies go through in determining a price is often archaic and arbitrary," says Pete Epple, senior director of Product Management for Zilliant. "Some businesses take the cost of a product and add margin on top of that price, while others simply match or better their competitor's offering. Another practice is what we call 'Out of Thin Air' or guessing."

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