CHAPTER

5

Pricing, Bidding, and Billing Projects

Pricing is a crucial factor in any business strategy, yet many fledgling business owners have little idea how to go about setting prices that are both competitive and profitable. This chapter explains how to develop your pricing strategy and introduces you to some standard methods for setting prices, whether your business sells services or products.

In addition, this chapter offers guidance for business owners who need to make bids to get work. Service businesses typically fall into this category, though sometimes product-based businesses also need to bid for jobs. This chapter also includes some general tips for the process and an outline for what typical proposals include.

On a cautionary note, be aware that antitrust laws forbid business competitors to fix, or even merely discuss, prices. For this reason, you won't find newsgroups or bulletin boards online where other businesses in a certain industry offer specific info on their pricing. Both online and off, pricing discussions among businesses in the same industry are not just taboo, they're illegal.

Directly sharing pricing info with competitors is illegal, but publishing general information about pricing guidelines is not. Good thing, since pricing is discussed first in this chapter.

SKIP AHEAD

Product sellers can skip ahead. Business owners who plan to sell only products don't need to deal with service-pricing or service-billing issues. If you don't plan to offer services, skip ahead to "Pricing for Businesses Selling Products," which discusses pricing for businesses that sell products.

Pricing and Billing for Service Businesses

Two major components of running a service-based business are setting prices and figuring out how to bill clients. Having rates that are well thought out is a key factor in soliciting clients confidently. And if you know the best way to bill them, you can manage your projects for maximum profitability and establish yourself as a true professional. This section explains these two essential tasks for service businesses. Once you understand what drives the pricing and billing processes, you'll find them much easier.

Setting Hourly Rates

Those who work as freelancers or own service-based businesses often find it difficult to figure out what rates to use. Many people struggle with assigning value to their time. Remember that your service rates are not just a measure of the value of your time—they also need to cover your overhead and yield your profits.

There's no single formula to put a price on your services, but there are a couple of common approaches. One formula is based on adjusting the number of billable hours so that revenue equals salary, overhead, and profit. And some businesses base their rates on what the market will bear. Each of these approaches is described in more detail below.

Billable Hours Formula

Many service businesses use a fairly simple formula to calculate their hourly rate. To keep it simple, look at this formula as if you're a solo freelancer without any employees:

   Desired annual salary
\+ Annual fixed costs (or overhead)
\+ Desired annual profit
÷ Annual billable hours
= Hourly rate

The gist of the formula is that it adds together all the money you want to bring in each year and divides that total by the number of hours you plan to work each year. The result is the hourly rate. This simple formula can be adjusted depending on the specifics of your business.

But first, it's a good idea to get a solid grasp on the concepts behind the formula.

- **Desired salary.** This is straightforward. How much would you like to earn annually? Include only salary here; desired profit comes later.
- **Fixed costs.** This is also a simple concept. How much will you spend each year on rent, utilities, office equipment, computers, and other items of overhead? As discussed in Chapter 4, fixed costs are independent of individual projects or services. You pay them regardless of how much business you're doing.
- **Desired profit.** You're in business to make a profit, not just to bring home a paycheck. A typical profit goal is 20% above salary and overhead (fixed costs).
- **Billable hours.** There's no single way to estimate this. Basically, the fewer billable hours you estimate, the higher your hourly rate will be; the more billable hours, the lower your hourly rate. A common way to approach this estimate is by calculating the number of potential billable hours in a year. With 52 weeks in the year and a 40-hour workweek, there are 2,080 potentially billable hours each year. Reduce that total by the number of nonbillable hours you expect to have—vacation, administrative work, or selling, for example. Just use your best estimate here. Very generally, the percentage of your time that is billable will probably be 50% to 80%. Much below that won't be very profitable, and higher than that usually isn't realistic. Use this percentage to determine how many billable hours you'll likely have each year. For instance, if 70% of your time will be billable, you will have 1,456 billable hours (2,080 hours x 70%).

Now add together your desired salary, fixed costs, and desired profit. Then divide that total by your billable hours. The result will be the hourly rate you'll need to charge to cover your fixed costs and bring in your desired salary and profit.

EXAMPLE: Samantha is starting a translation service and wants to figure out her hourly rate. She sets a first-year salary for herself of $30,000 per year and estimates her annual fixed costs to be approximately $25,000. This totals $55,000 for salary and overhead. A 20% profit brings the total to $66,000. Samantha thinks she'll have to spend a good amount of time doing sales and getting her business off the ground, so she figures only about 60% of her time will be billable, resulting in 1,248 available billable hours. By dividing her salary, fixed expenses, and profit ($66,000) by 1,248 billable hours, Samantha sees that her hourly rate should be $52.88. She rounds that up to $55 per hour.

	Salary	$30,000.00
+	Fixed costs	25,000.00
	Total salary & fixed costs	55,000.00
+	20% profit	11,000.00
	Total salary, fixed costs, & profit	66,000.00
÷	Billable hours	1,248
=	Hourly rate	$ 52.88

Setting Market-Based Rates

Another way to set your hourly rate is to throw the formula out the window and simply set your rate for what the market will bear. Beware that this might not yield a profitable hourly rate, because you're not basing your rate on the actual numbers you'll need to achieve. On the other hand, it may be more likely to deliver a rate that customers will accept.

If you base your rates on the market, use any market information you can get to guide you—including what competitors charge, industry standards, and your own experience of using various rates. If you constantly fail to snag clients once you provide a quote, that's a sign your rates may be too high. On the flip side, if you get every job you bid on, you could probably get away with nudging, or even shoving, your rates upward.

It's not a bad idea to use a combination of the formula-based and market-based approaches. Using the formula will help ensure that you set a rate that is profitable, and using the market to adjust the rate up or down will help you stay competitive. For example, if the formula yielded an hourly rate of $45, but other similar businesses charged $65 to $75 per hour, you could feel comfortable increasing your rate to $55 per hour, making your business a bargain while still turning a profit.

FORM

Billable Rate Worksheet. The Nolo website includes a downloadable interactive worksheet to help you calculate an hourly rate for your service business. See Appendix B for the link to this worksheet and other forms in this book.

TIP

It is legal to research and use competitors' rates. The antitrust laws mentioned earlier are intended to protect consumers by maintaining competition in the marketplace. The laws are supposed to prevent anticompetitive agreements among competitors to set prices at a certain level. On the other hand, setting your rates to position your business among similar businesses is perfectly legal, so long as you obtained your competitors' pricing information from another source, not directly from them. After all, researching the market and setting prices accordingly is the essence of competition.

Billing Options

Service businesses and freelancers typically use a variety of billing options to accommodate different types of projects and clients. Common billing options include flat fees, hourly billing, and retainer arrangements. Each of these options is discussed below.

Flat Fees

With flat fee billing, you and your client agree to a total fee for a specific project. In the right situations, it is efficient and professional to charge your client a flat fee for your services. The fee should roughly reflect the number of hours you'll work multiplied by your hourly rate. Contractors typically discount their hourly rates for larger projects.

How to Use the Billable Rate Worksheet

To use the billable rate worksheet on the Nolo website, follow the steps outlined below. Each step is explained in greater detail later in this section. Enter figures into only white cells; do not enter anything in blue cells.

Step 1: Enter your desired annual salary. This is your take-home pay, not your overall business profit.

Step 2: Enter your estimated annual fixed costs. (For more on estimating fixed costs, see Chapter 4.)

Step 3: Enter a profit goal for your business as a percentage by which you want to exceed salary and fixed costs. A 20% profit goal is typical.

Step 4: If you know how many billable hours you plan to perform in a year, enter that amount. Or, if you're not sure how many billable hours you plan to work in a year, you can work backward by estimating the number of *nonbillable* hours you plan to spend—such as on vacation or doing administrative work—and subtracting those hours from the total number of possible billable hours in one year (2,080). The worksheet asks for your estimated nonbillable hours of various types for time periods that are easiest to estimate (for instance, vacation is estimated in weeks, while administrative work is estimated in hours per day), then converts those figures into annual hourly amounts. If you enter figures both for your estimated billable hours and estimated nonbillable hours, the calculator will use the first figure, estimated billable hours.

Result: The worksheet will show you what hourly rate you should charge in order to make your desired salary, cover your fixed costs, and make your desired profit, assuming you work the number of billable hours you estimated.

Billing per project usually makes clients happy because they know up front what their costs will be. Project-based billing can also benefit you. A flat fee encourages efficient project management and reduces the hassle of tracking and billing for your hours (though you should always keep track for your own records).

However, flat fees aren't the best idea for every project. You will feel underpaid if it takes much more work to finish a project than you expected, and the customer will feel overcharged if the project takes much less time than you estimated. If you want to bill per project, it's crucial that you and the client both understand and agree on the project's exact scope. In fact, this agreement should be reached even before you quote a fee. Once the client accepts your fee, the project details should be outlined in a contract. Payment terms can vary, but contractors typically require a deposit up to one-half of the total fee on signing the project contract.

Sometimes it's not possible to pin down a project with specificity at the outset. Some clients simply don't want to hammer out all the details. Other times, a short deadline makes it difficult or impossible to carefully consider all aspects of the project before you start work. In these cases, you're asking for trouble if you set a flat fee.

Suppose, for instance, that a client calls and needs a new section developed for a website ASAP. The owners of the site desperately want you to start immediately, but you have only a vague idea of the work involved. A flat fee here would be a really bad

Charging for Outsourced Services

Sometimes service businesses need to hire another contractor (typically called a subcontractor) to get a job done for a client. You can charge your client for the subcontractor's work in different ways. You can simply charge your standard hourly rate for all work completed, whether your company did the work or a subcontractor did. This approach can work for or against you, depending on what you pay the subcontractor. Under a common second approach, businesses mark up the cost of the subcontractors and bill the client accordingly. Businesses vary a lot in how much they mark up subcontractors' rates. I've seen 10% markup and 100% markup. You'll have to decide what seems fair to your client and profitable to you.

Sometimes the client will hire and pay the sub directly, without a markup. This can work if that piece of the work is discrete, or distinct from the rest, and the client is responsible for supervising the sub's work and has appropriate liability insurance. However, many contractors prefer to choose and supervise all workers on the same project, for many reasons: They like to have total control over the project, they like to choose subcontractors whose work they trust, they usually make a fair profit on the subcontractor, and it simplifies the project as well as the contractor's potential liability to the subcontractor and the client.

In any case, let your client know in advance whether you plan to use subcontractors on a project, especially if the subcontractor is a highly skilled specialist and the rate you bill for the subcontractor will be higher than your standard rate. Clients never like to be surprised with bills higher than they expected.

> **EXAMPLE:** Glenn is a construction contractor with a standard hourly rate of $85 per hour. When hired for a remodeling project, Glenn tells his client he will need to hire a few subcontractors over the course of the project who may have rates higher or lower than his. Glenn and the client come to the understanding that they'll agree to all subcontractors and their rates before Glenn hires them. When it's nearly time to bring in a plumber, Glenn tells his client he'd like to hire Khalsa, whose rate to the client will be $103 per hour. Khalsa's own rate is $90 per hour, but Glenn marks up the rate by 15% to $103 so that he can make a reasonable profit for managing Khalsa on the project.

idea—the project could take much longer than you expect, leaving you to do the work for an unfairly low flat rate.

If the project isn't carefully outlined before you start, forget the flat fee—hourly billing is probably the safest way to go.

Hourly Billing

Billing clients by the hour is pretty straightforward. You keep track of how many hours you work, and bill the client accordingly. As explained above, you should use this type of billing—also called "time and materials billing"—in situations in which the project isn't well defined.

While billing by the hour will protect you from being underpaid for a poorly defined project that takes more time than you thought it would, the client will never be happy if you present a huge, unexpected bill. Even when you choose hourly billing for a project without a clear scope, do your best to work efficiently, communicate with the client, and avoid handing over a surprising bill.

Keep in mind that it is up to you to demonstrate your value to the client, explaining why your hourly rate is justified and how you spent your hours. Even if you can't define the project specifically enough to set a flat rate, do your best to estimate how long the project will take, and try to keep your hours within your estimates.

TIP

Set reasonable hourly increments when billing. For instance, will you bill the client a full hour for work that takes you 20 minutes to finish, or for a five-minute phone conversation? This approach is generally not recommended because clients see it as unfair. Many people use increments of 15 or 30 minutes for billing purposes. It can be good public relations to show some short phone calls on the bill with no charge attached. That makes the client feel better about the times you round up to the nearest 15 minutes for other tasks.

Jennifer F. Mahoney, owner of an illustration service in Northern California:
It's helpful to learn about the accounts payable process for each client and to understand who in the company releases checks. It's often an entirely different person or department from the one who calls you to offer work. You don't necessarily want to strain your relationship with the person who calls offering you work just because a different department of the business doesn't pay on time. Pave the way for timely payments as much as possible by getting to know the correct procedure, and when it's time to press for payment, you'll know the right person to call.

Retainer Arrangements

In a traditional retainer arrangement, the client pays an ongoing fee, usually monthly, to keep the contractor "on call" for certain services. Retainer arrangements are usually best for clients with regular and predictable needs—for example, maintaining a law firm's website, providing maintenance services for an apartment building, sewing and tailoring costumes for a theater, or doing public relations for a ski resort. As with flat-rate billing, you should always define the amount and scope of services expected of you under a retainer arrangement.

In some professional businesses, especially law offices, a "retainer" is requested at the outset that is really a deposit, or a prepayment of fees and costs, usually under a written fee agreement. Lawyers also sometimes use the traditional monthly-fee retainer described above.

Bidding and Creating Proposals

Sometimes it's not possible to sell a service or product just by offering it to the public for a certain price. Many service businesses (and some businesses selling products) must submit a bid or a proposal on a project to be considered for the job. (The terms "bid" and "proposal" are often used interchangeably.) If the client accepts the bid, then a contract is typically executed to confirm the sale.

Because bids can make or break a sale, you should take care when putting one together, both with the contents of the bid and its physical appearance. Often, the hardest part of bidding is breaking down the project into smaller parts so that you can make good estimates of how much work, time, and materials it will require. Once that's done, it is usually quite easy to write the proposal. This section outlines how to put together a bid to help ensure your chances of success.

SKIP AHEAD

When you don't need to get it in writing. Businesses selling products usually don't need to worry about bids or proposals. If you don't need to learn about the bidding process, skip ahead to "Pricing for Businesses Selling Products."

TIP

When a proposal becomes a contract. A proposal usually converts to a contract when a client accepts your terms. In practice, however, you should suggest that you sign a separate contract to finalize the agreement with the client. This is partly because it's an opportunity to make sure the client truly understands what you said in your proposal. It's also a good idea because there are things you should cover in a contract that you wouldn't necessarily put in a proposal, such as who provides the insurance, how you will handle extras or change orders, specifics of each side's remedies for breach of contract, which state's laws apply, and whether you will mediate or arbitrate any disagreements. (See Chapter 10 for an in-depth look at how to use contracts in your business.)

Get All the Information You Need

You won't be able to make an effective bid on a project until you thoroughly understand all the details involved. Ask the prospective client as many questions as necessary to flesh out the full scope of the project. A prospective client who's putting a project out to bid among competitors may already have a sheet of specifications, but if you have questions, ask them.

Often, the client will want to be involved in certain aspects of the project, so it's important you both agree who will take a primary role in various tasks or duties. You should hash out the breakdown of duties and workflow right at the beginning.

Break Down the Project and Make Estimates

Next, break down the project into manageable components and estimate how much time, labor, and materials you'll need for each one. This is generally the best way to make accurate estimates.

For instance, your head will spin if you try to estimate how long it will take you to complete an entire landscape design project. But once you break the project into parts—grading, spreading gravel, paving, planting trees, and so on—making estimates for the individual bits won't seem nearly as overwhelming.

Multiply the number of hours you expect the project to require by your hourly rate. It's common for freelancers to lower their hourly rates a bit if the project is a large one. This is reasonable, because it's usually more profitable for a freelancer to work consistently on one project than to work piecemeal on several smaller projects.

Sometimes however, freelancers are tempted to lower their estimates out of fear. After adding up all the hours needed for a large project and multiplying this by their normal hourly rate, they think the fee looks too high and start slashing it to make it more acceptable to the client. Guard against this temptation. It's fine to reduce your hourly fee slightly when you anticipate efficiencies on a large-scale project, but don't sell yourself short just to get the job. Not only will you regret it after you've worked long hours on the project for an unreasonably low fee, but you'll fail to earn respect from clients if you don't ask for the compensation you are worth.

Consider Expenses

Who will be responsible for expenses incurred during the project? The answer varies from project to project; there are no hard and fast rules. Typically, contractors are responsible for covering their own normal expenses of doing business. (However, this is not always true. Attorneys, for example, commonly bill clients for copies and telephone calls.) Clients usually bear printing and production costs, as well as any costs that aren't typical to the contractor's business such as travel, international phone calls, or equipment rental fees.

In any case, you and the client should agree in advance who will cover which expenses. In addition, make sure to address whether there are any limits on reimbursable expenses or whether the client must approve expenses in advance. Also nail down how you will bill the client for expenses.

For example, travel expenses are quite often billed to clients. It's wise to make a specific breakdown of the expenses that will be covered, such as airfare, rental car, lodging, taxi, train, parking, and food.

TIP

Proposing reasonable limits on client expenses. Even if your client has deep pockets and seems willing to cover whatever expenses you incur, you should offer some limits on reimbursable expenses. This will help to head off any potential conflicts or unpleasant surprises over reimbursement bills. It also shows the client that you care about giving a good deal.

You can handle payments for expenses a number of different ways. A few possibilities are discussed below.

- **Set an amount that the client will pay, regardless of the amount actually incurred.** For instance, you and the client can agree that the client will pay $1,000 to cover all travel costs. If your actual costs are lower, the extra money will be yours; if higher, you'll eat the difference.
- **Bill the client for actual expenses incurred.** You can do this with or without a cap. For instance, you could agree that the client will reimburse you for all actual travel costs. Or, you could agree the client will reimburse you for actual travel costs up to $500.
- **Set a per diem rate for certain expenses.** "Per diem" simply means "per day." Food is typically billed at a set per diem rate—say, $50 or $75 per day.

EXAMPLE: Samantha is working on a bid for a translation project that will require her to travel to Brazil three times. Her client, Bahia Travel Company, says it will cover travel expenses and asks Samantha to draft a proposal specifying the terms. Samantha drafts the following terms regarding travel expenses, which she will include in her proposal:

"Samantha will be responsible for all expenses involved in the project, except for travel-related expenses, which Samantha will bill to Bahia Travel Company monthly, as follows:

Airfare. Billed as actually accrued, including all taxes, not to exceed $1,500 per round-trip ticket. Tickets will be economy class.

Rental car. Billed as actually accrued, including insurance and taxes, not to exceed $50 per day.

Lodging. Billed as actually accrued, including all taxes, not to exceed $175 per night.

Food. Billed at $75 per day.

Taxi. Billed as actually accrued.

Parking. Billed as actually accrued."

Write Your Proposal

Once you've finalized the important details of the project, it's time to put together your proposal. Your goal is to present all important information clearly and to demonstrate you have a solid plan for getting the job done right. Proposals should always be professional and somewhat formal in tone, but don't be afraid to let your personality show. If you feel stiff, you won't usually have a better bid, just a more stilted one.

> **Clare Zurawski, Albuquerque Regional Manager of WESST, a New Mexico nonprofit dedicated to helping people start or grow their own businesses:** *A thorough, fair, and clearly presented proposal is a sure way to impress your would-be clients with professionalism, and paves the way for effective communication going forward.*

Some project proposals are two to three pages long; some exceed 20 pages. There's no hard and fast rule here. You should use as much space as it takes to outline the project details with adequate—but not excruciating—detail. An outline for a project proposal might go something like this:

- **Project overview.** Describe the big picture, including relevant details about the client and an overview of the project.
- **Project objectives.** Include detailed information about the project, including all the different components of the project and how they fit together.
- **Proposed approach.** Describe how you would approach the project and how you would achieve the client's goals. Be specific, and don't assume that the client knows anything about how you do your work.
- **Specific responsibilities.** Outline what you understand your specific responsibilities would be.
- **Deliverables.** This is a term for the specific products that your work will yield. For instance, deliverables might include a 20-page written report, a set of tax documents, or a 100-page travel guide.
- **Timetable.** Scheduling is always an important part of project management, so you should always outline when you expect certain parts of the project will be completed.
- **Fee and payment terms.** In stating your fee, you don't have to explicitly state your hourly rate or how you arrived at your amount. Simply make it clear that your fee is based on your understanding of the project requirements as outlined in the rest of the proposal.
- **Expenses.** Outline whatever agreement you and the potential client have regarding who will cover which expenses.
- **Conclusion.** Wrap up the proposal. Strive for a professional tone that expresses your enthusiasm for the project. Though some proposals serve as the project contract once the client has accepted them, you will usually say here that you expect to sign a separate formal contract.

Pricing for Businesses Selling Products

As with pricing services, there are different ways to figure out what to charge for the products that your business sells. Of course, your cost of acquiring or making the products will play a big part in your pricing decisions. But you may have difficulty deciding on an appropriate markup. This section will walk you through a few issues to consider when pricing goods.

CAUTION

Don't discuss your product pricing strategy with competitors. Antitrust laws forbid you to fix prices with your competitors and even to share price information or discuss prices with them. Steer clear of this potentially serious legal trouble by simply avoiding pricing discussions altogether.

Establish an Overall Pricing Strategy

Before deciding how much you'll charge for your widgets, you should think about and adopt an overall pricing strategy for your business. Keep in mind that the very same widget might be sold for $0.99 at your local 99¢ store, $5 at a chain retailer, and $25 at a swank boutique. The price can vary so much because each of these stores has its own pricing strategy—and you should, too.

The concept is simple: Will your business use a high-end, middle-end, or low-end strategy? Each strategy can be profitable if you work within its logic. Here's a quick description of how each strategy typically works.

- **High-end** shops can charge high prices so long as they offer something in return, such as a great selection of hard-to-find or highly specialized products, extraordinary customer service, an exclusive atmosphere, or simply top-notch quality.
- **Middle-end** shops charge average prices and succeed on the basis of other factors such as selection, customer service, and convenient hours and locations. None of these factors are exceptional enough to justify high-end prices, but they're attractive enough to draw customers who aren't necessarily looking for the very lowest price.
- **Low-end** shops succeed by forgoing some amenities such as a reliable selection or a convenient location. They attract customers by offering the lowest prices. Customers might have to paw through bins of merchandise or drive across town to a cold, cheerless warehouse store, but they'll do it because they know they'll get a bargain.

Whichever strategy you choose, it's important that you stick with it and use it consistently. You will confuse customers and push them to your competitors if you offer a confounding mix of high- and low-end items in the same store.

Research Markup Data

Once you've got your pricing strategy in place, you must decide how much you'll mark up your products for sale. You can set your prices appropriately after you do some research to figure out how much other similar businesses mark up their goods.

One easy source of markup information is simply the manufacturer's suggested retail price or MSRP, also called the suggested list price. If you buy a line of floor lamps that cost you $30 per unit and the MSRP is $90, then you know the manufacturer is recommending a markup of 200% of cost. You don't have to follow the recommendation (the days of adherence to MSRPs are over), but you'll get a good idea of what may be typical in the marketplace for that item.

In addition to using MSRPs, ask your manufacturers and suppliers for information they may have on average markup rates. Your suppliers can be a valuable source of this kind of information, beyond setting MSRPs for each product.

You can find good information about industry standard markup rates in many sources. Trade associations and journals may give you valuable data. Directories and guidebooks are also available on many industries. These books tend to be expensive ($100 and up) but are often treasure troves of valuable industry info. Hoover's Inc. is a company that specializes in providing comprehensive market data; its website (www.hoovers.com) offers a wealth of information and publications for sale. Many of the titles offered at Hoover's are from Plunkett Research, another firm specializing in market data. Plunkett has its own website at www.plunkettresearch.com.

Don't stop there. Do your own research, and look specifically for info pertaining to your type of business. Search online, visit the library of a local business school, ask local trade associations, and generally do some sleuthing to turn up the data you need.

What's Up With Markup?

Markup is the amount that's tacked on to the cost of an item to arrive at its selling price. For instance, a wristwatch that cost $25 to the retailer may be marked up by $37.50, for a selling price of $62.50. What can be confusing is that markup rates are sometimes expressed as a percentage of cost, and other times as a percentage of selling price.

For example, the markup percentage for the wristwatch is 150% of cost or 60% of selling price. What does this mean? The percentage of cost calculation works like this: The cost of the watch ($25) is multiplied by 150%, resulting in a $37.50 markup, which is added to its original cost ($25) to arrive at the selling price of $62.50.

Here is the percentage of selling price calculation: The selling price ($62.50) is multiplied by 60%, resulting in the same $37.50 markup arrived at with the percentage of cost calculation. As you can see, these two different ways of expressing a markup percentage yield the same result.

When you search markup rates, be sure you know which type of percentage you're dealing with: percentage of cost or percentage of selling price. If you apply a percentage of selling price markup rate to the item cost, or use the percentage of cost markup with the item's selling price, you'll end up with the wrong result. For instance, if you mistakenly calculate the wristwatch markup by multiplying the item cost ($25) by the percentage of selling price markup rate (60%), you'll end up with a markup of $15, and a selling price of just $40.

Chapter 5 Checklist: Pricing, Bidding, and Billing Projects

- ☐ Never discuss the topic of pricing with competitors—basically, anyone in the same industry as you.
- ☐ If you're in a service business, set hourly rates carefully, by using a formula, basing the rates on market conditions, or a combination of these approaches. However you set your rates, remember that you'll need not only to earn a salary but also to pay for your overhead and make a profit.
- ☐ If you're in a service business, become familiar with various ways to bill clients and understand which methods are best for specific situations.
- ☐ If you will have to bid for work, learn how to put together a professional proposal.
- ☐ If you plan to sell products, develop an overall pricing strategy to guide pricing decisions.
- ☐ If you sell products, research the market to understand what typical markup rates are used by others in your industry.