



Driving Revenue: Value, Value Propositions and Value-Based Pricing

BY ARTICULATING YOUR FIRM'S VALUE, your company will be able to create value propositions and a value-based pricing strategy that will enhance the firm's revenue and profit.



PATRICK JOHANSEN,
CLM, CPP
Director of Business
Development
Brinks Hofer Gilson & Lione
Chicago, Illinois

Alan Weiss said it best: "Every buyer wants to lower fees, but not one wants to lower value." Not only does this truism encapsulate the challenge of serving clients, it reveals a law firm's true business objective: offering value. In a capitalist economy, every consumer – whether conscious or not – asks the question: "Is this purchase worth the cost?" In other words, is the value of the purchase equal to (or greater than) the price paid? Every transaction is based on this type of cost/benefit analysis.

Prospective clients have four cost/benefit options when selecting counsel: choose you, choose a competitor, do the work in-house or do nothing. Why choose your firm? A singular – but not simple – reason: value. Because the essence of your client relationships – acquisition and retention – is rooted in the concept of value, it is imperative that you and your firm be proactive and deliberate in defining your firm's value.

VALUE DEFINED

In essence, value is what a firm provides to a client over and above the client's expenses. By agreeing to hire you, your client believes that your services (their benefits) will be worth more than your billings (their cost). Here is a simple formula for calculating value:

$$\text{Value} = \text{Benefits} - \text{Cost} (V=B-C)$$

Just as clients use this formula (consciously or unconsciously) to determine your value, your firm and you need to do the same. What benefits do you provide to clients? What do you charge clients? Are your benefits worth more than your costs?

This concept is the basis of competitive advantage, according to Harvard Business School Professor Michael E. Porter, and the reason value is so critical to your firm's revenue and profit. "Competitive advantage grows fundamentally out of value a firm is able to create for its buyers that exceeds the firm's cost of creating it," wrote Porter (*Competitive Advantage*, 1985).

To maximize your clients' value, you must focus on four unique – but interrelated – elements of the value formula: cost, differentiation, competitive intelligence and client expectations.

COST

Cost is half of the value equation, so it is critical to determining value. There are two equally essential parts to consider: first, how much it costs you to provide your services, and second, how much you charge clients.

Lawyers are usually proficient in calculating their costs; it is half of the firm's income statement. In the wake of the Great Recession, however, cost-cutting measures could go only so deep. To improve (i.e., reduce) the cost of providing services, firms are exploring issues of efficiency, legal project management (LPM) and legal process outsourcing (LPO).

At the same time, firms have been faced with client push-back on billings. When clients do not see their benefits rise, they can (and will) push their costs down; as costs fall, value typically rises. Larger firms have responded by hiring pricing staff, especially with increasing requests for alternative fee arrangements (AFAs).

To maximize value, firms need to understand the delivery of service behind their fees and, more importantly, how their fees affect their clients' costs. In addition, they need to appreciate that cost is only half the equation.

DIFFERENTIATION

Differentiation is one of the three "benefits" components, but it tops the other two in importance. Differentiation is the power to stand alone. It is developing unique attributes, or value activities, that are valuable to your clients and that cannot be matched by your competitors. This raises your benefits score. In a law firm, differentiators can be tangible (e.g., client list, industry niche, experience, clever

advertising) and intangible (e.g., reputation, level of service). Assessing your firm's strengths and weaknesses help define your value activities.

Before the 1990s, law firms relied on their reputations to differentiate one another. In the last two decades, the growth of legal marketing has created a plethora of differentiation strategies: industry, geography, practice, service, etc. Too often, however, marketing efforts slap cute slogans on value activities, reducing a key competitive advantage exercise to mere marketing fluff.

Cost and Differentiation are enough to get your firm to define its value. But take note: The next two components will ensure that your value creates true competitive advantage.

COMPETITIVE INTELLIGENCE

There is only one sure way to know if your differentiation is truly unique and your costs are truly reasonable: competitive intelligence.

Any successful law firm today needs to know where it stands in the marketplace. More importantly, for the firm that seeks to maximize its value, an analysis and an appreciation of the competition is a must. Conducting research on your competitors and identifying industry benchmarks is crucial to your efforts.

In many respects, the rise of the business development function in law firms is tied directly to firms defining their value. A firm cannot know the breadth and depth of its benefits without knowing what its competitors are offering.

CLIENT EXPECTATIONS

As a former chairman of Ford Motor Co. once said, "If we aren't customer-driven, our cars won't be either." Ultimately, a law firm's value rests with its clients. Implicit in a firm's value formula, therefore, must be an understanding of client expectations.

Said differently, client feedback needs to be one of your firm's ongoing priorities. The following three questions are critical to understanding your clients' perceived value:

- What is the value of our firm to the company?
- What benefits are gained by working with our firm?
- Are our fees reasonable?

Each question illustrates one of the three components in the value formula. By matching your clients' answers to the appropriate component, your firm will be able to understand,

Nothing can help your firm reduce its costs, articulate its uniqueness or win new business better than defining your firm's value.

then improve, its client relationships. If you are hesitant to ask about your fees, remember this: Clients are not price-sensitive; they are value-conscious.

Once you have been able to understand your costs, your competition, your differentiation and your clients' expectations, you are ready to build a case for your value. The way in which you communicate your value is called a value proposition.

VALUE PROPOSITIONS

In his book, *Winning the Professional Services Sale*, Michael McLaughlin highlighted the importance of communicating value: "A superior understanding and expression of value can edge out a formidable opponent with a long-standing client relationship."

McKinsey & Co. developed the concept of the value proposition in the 1980s. A firm's value proposition helps articulate the firm's benefits, with the goal of all benefits outweighing the cost (remember the formula: $V=B-C$). Here is a simple definition: *A value proposition is a reason why a client will benefit from engaging the firm.*

Value propositions are built on the three benefits components. Differentiation will offer firms the largest number of options, as well as the most focused. Competitive intelligence will provide the context for knowing which propositions are truly unique, which are shared by only a few competitors, and which are too common to pursue. Client expectations – the voice of the client – will tell you which are the most important for client retention.

VALUE-BASED PRICING

A final step in maximizing your firm's value is to consider adopting value-based pricing. Historically, law firms have followed the 90-year-old model of hourly billing, also known as cost-based pricing. Hourly billing uses simple math to calculate the firm's costs, but it cannot predict volume or realization, nor does it focus on the worth of your firm's benefits to a client.

More recently, as competitive intelligence has become more available and lateral hiring has become more prevalent, law firms have better knowledge to employ competition-based

pricing. Although this helps your firm maintain relative parity with other firms, it cannot predict volume or realization, nor does it take into account another firm's cost to provide services. Most importantly, it does not focus on the worth of your firm's benefits to a client.

Value-based pricing (VBP) is a pricing strategy centered on clients and focused on maximizing a client's value and a firm's profit.

VBP starts by understanding what the client values. Next, VBP determines if any firm benefits match the client's need, and if so, the best pricing for the firm's services. Third, VBP evaluates the most cost-effective way to deliver those services. Finally, the firm delivers its services and monitors its progress to ensure profitability.

By defining your value and value propositions, you have covered two of the three key principles necessary to achieve success with value-based pricing: comprehending and communicating the value to your clients.

The final key – convincing your clients that the value is worth your fee – falls to your attorneys. They are the firm's sales force. They are the ones who bring new matters to the firm by cultivating relationships with clients. They are the ones who will use the firm's value propositions like arrows in a value quiver. Attorneys are the key to driving revenue.

A VALUE TEST

Nothing can help your firm reduce its costs, articulate its uniqueness or win new business better than defining your firm's value. A recent Harvard Business Review article challenged B2B companies "to build a robust case for the superior value of their solutions." Are you ready to test your firm's value? ■

About the author

Patrick Johansen, CLM, CPP is the Director of Business Development at Brinks Hofer Gilson & Lione. He is a former member of the ALA Greater Chicago Board of Directors and the Legal Marketing Association Chicago Board of Directors. He blogs at www.patrickonpricing.com.