

Fiscal 2023 Rate Strategies Series: Big Miss #1 – Unnecessary Discounting

By [Mark Medice](#) on October 16, 2022

As we look to close out 2022, it has never been more important to execute your pricing strategy well. The competitive market for law firms may be heading into a more challenging time compared to the past five years, and it will be even more important to get rates right in the face of upcoming storm clouds.

Law firms have progressed through the pandemic cycle with grace, with financial results surpassing most expectations. During this time, firms have fought Covid, battled talent wars and inflation, embraced remote working patterns, and managed geopolitical conflicts on many levels.^[1]

But the current economic news cycle continues to sound the drumbeat of a slower economy. As a result, some economists believe that we will finally pay the piper for the easy monetary policy that began back in the credit crisis of 2008 and carried through the pandemic with fiscal stimulus, causing inflation.

Economic headwinds may cause law firm management to pivot away from progressive pricing strategies, which would be a big mistake. Instead, during these times, firms should focus more on pricing execution to support delivering value to clients and retaining their best talent.

As you plan for fiscal 2023, I encourage you to think strategically about pricing with particular emphasis on avoiding the three common pricing mistakes (i.e., *the big misses*), which I will cover in the coming weeks, starting today.

In the final post, I will offer you a checklist and scorecard that you might use to ensure you avoid the big misses and prepare for a successful FY23 pricing experience.

For this week, I will review the **magnified effects of unnecessary discounts**.

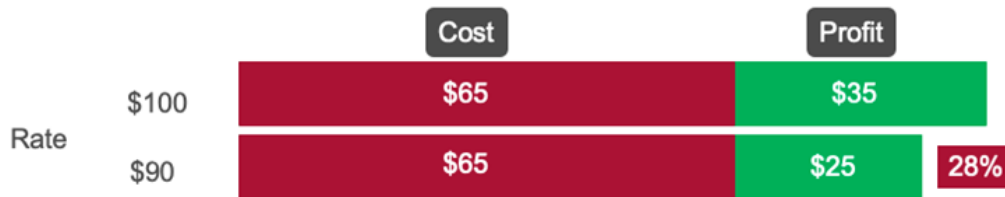
Big Miss #1: Unnecessary Discounts and the 3X Rule

Discounting sometimes is necessary, and if it were an occasional justified event, that *might* be acceptable. But undisciplined discounting serves as a financial headwind accompanied by magnified effects on the bottom line **around three times the discount**.^[2]

Importantly most lawyers don't understand this 3x rule. It works as follows:

Imagine your rate is \$100. Let's say your direct and overhead costs are \$65, leaving you with a \$35 profit. But then you discount by 10%, resulting in a \$90 rate. That reduction doesn't reduce your costs, so your profit is now $\$90 - \$65 = \$25$. That lowers your profit by ~30% (i.e., $\$35 \rightarrow \25). Essentially your 10% upfront discount is magnified approximately **three times your discount** on the bottom line.

The visual below illustrates this idea:



How to Reduce Unnecessary Discounting

1. Educate your lawyers on the mechanics of the above. Tell them that discounts don't help your clients but harm them if you undervalue your services. You can't attract and keep good people if you don't have profits. If your client pays below fair value, that may seep into the quality of your legal services.

2. Teach Value Discovery. Help your lawyers understand market value and your firm's intended position in the market. You should be able to answer direct questions related to the desired position, like:

- How do we establish our client position? How do we learn what is important to the client to differentiate our firm?
- Do we intend to be a premium provider? (*Note: Few firms are structured to be discount providers, so that isn't an option here.*)
- What are similar rates for **true** competitors in the marketplace?
- Are we pushing rates to the top of the market for our leading partners?

3. Systematize. Lawyers tend to discount up to the discretionary boundaries provided. So provide tools and data to help them discover value and systematize discounting processes to guide lawyers to price effectively while teaching them client negotiation strategies. Provide a guidance system to avoid habitual discounting patterns.

The bottom line is unnecessary discounting helps no one and hurts everybody with an 'x multiple' to your bottom line. Avoid this at all costs and create a culture for pricing well with your clients.

In our next installment of this series, we will discuss rate stagnation and pricing trends for fiscal 2023.

^[1] *Global law firms have dealt with this directly with office closures, exchange rate volatility, and humanitarian aid, but all firms have had to deal with increased cyber risks, inflation, and uncertainty.*

^[2] *Note that the 3x rule depends on your margin. If your margin is lower than 30%, then the multiplier is actually higher than 3 and can be quite large to the point of being unprofitable.*