

How To Realistically Set Your Fees - Part 4

By Chuck And Sue DeFiore

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Effect Of Bad Debts

So far, we have covered the major factors involved in setting your fee structure. We have set a realistic number of billable hours, calculated the effect of expenses and taken into account the cost of a benefit package.

This has brought us to an hourly rate of \$77. By charging \$77 per hour, you will have an income of \$46,000 per year, plus benefits.

What happens when you have a client that does not pay you for your services? What happens if a customer goes out of business before your invoice is paid? How will these events affect your own planning? Do you want to take a bad debt write off on your taxes? Do you want to try to include for these contingencies in your fee structure? Your answers to these questions will have a direct impact on how you operate your business.

Thankfully, unless you provide very poor service, most clients will eventually pay you. However, it may take you awhile to collect your money and you may have to settle for less than the originally billed amount. You have the option of adding late fees to your invoices, but keep in mind, the more time you spend trying to collect a past due invoice, the less time you have to devote to paying customers. Also, if you need to engage an attorney or collection agency, you will in all likelihood, not see the full amount of your invoice because of their fees.

One way in which you can protect yourself is to build into your fees an allowance for bad or uncollectable debts. If you estimate that 5% of your invoices will be either unpaid or underpaid, then add 5% to your hourly rate. For example, your hypothetical fee is now \$77 per hour, 5% of that is \$3.50, added together gives you a rate of \$80.50 per hour. If we round this off to \$80, you would have approximately \$3300 per year cushion.

Allowing 5% for bad debts may seem high, however, keep in mind the present state of the economy and remember this figure can be adjusted as the economic conditions change. Today, it is not unusual for businesses to take longer to pay invoices than they did a couple of years ago. Most businesses expect to pay late fees for overdue invoices, however determining how much to charge and whether or not you are meeting the various legalities involved can be time consuming. It may be easier to add a percentage to your overall fees to offset bad debt. In a sense, you are spreading the economic risk over all your clients. For a small business this may be the safest and less time consuming course of action.

If your client base is large enough, a certain percentage of your customers will go out of business, leaving you with unpaid and uncollectable invoices. There is little chance you will collect any money in a bankruptcy hearing. To protect yourself, you can charge partial fees as your work progresses. This way you are assured of having received at least some of your money. Not all businesses are set up to take advantage of this option.

Remember, you are not in business to give away your services. Your goal is to provide yourself and/or your family with a reasonable income. Uncollected invoices are part of doing business, you owe it to yourself to consider this before you get stuck.

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