

Starting a Consulting Business (2002)

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The diversity of the HIM profession provides consulting opportunities in a variety of practice settings and areas of expertise. The decision to start a consulting business requires thoughtful planning particularly in areas that are not core skills of an HIM professional. This practice brief walks through the critical steps to consider when starting a consulting business.

Developing a Business Plan

The first step in starting a consulting business is one that is often skipped. Developing a business plan not only provides a guide but also forces an individual to consider all aspects of starting and running a consulting business. Consultants must identify the expertise they have to “sell,” the services clients would likely “purchase,” and the potential market for business development. A variety of resources are available on the subject, including books and software programs that can assist with developing a business plan.

Other helpful resources are the local chapters of the Small Business Administration (SBA). The SBA offers assistance in business development and can help identify financial resources. If you are planning a business that requires start-up or expansion capital, a formal business plan is a basic requirement for qualifying for a small business loan.

Evaluating Education and Experience

Your education level, credentials, and years of experience should be relevant to the type of consulting expertise offered to clients. Successful consultants strive to become the most knowledgeable in their area of expertise. As a general guideline, an individual should have at least two years experience in the HIM field related to the area of expertise, particularly if the consultant will offer advice on management issues, HIM standards of practice, regulations or standards, coding, policy and procedures, or billing and reimbursement.

There will be situations where practitioners with less experience may function as consultants. In this situation, the type of work they perform should be commensurate with their experience. For example, they may provide interim or vacation coverage or work as part of a team under the direction of a more experienced consultant. The years of experience and expertise offered to a client often affect the rates charged. A consultant with little or no practical experience in a specific area of expertise cannot expect to charge the same rates as those with extensive experience.

Consultants in the HIM field should be credentialed and active members of AHIMA, which demonstrates awareness of current professional issues. Developing a professional network (both locally and nationally) is important to staying current and on top of the field.

In addition to education, experience, and advanced training, there are a number of personal characteristics common to professionals who succeed and enjoy consulting. See “Profile of a Consultant” below for a description of those characteristics.

Profile of a Consultant

Following are common personal characteristics of successful consultants.

- good listener
- objective
- tactful
- professional
- visible/involved in professional activities
- ability to work on a variety of unrelated tasks

- politically savvy
- sense of humor
- organized
- stamina
- self-motivated
- self-disciplined
- positive attitude
- team player
- ability to work with all levels of people
- excellent written and verbal skills
- speaker/teacher
- ability to build and manage relationships
- ability to implement change

Creating a Business Structure

Once a business plan has been established, the next step is to determine a structure for the business. Legal and accounting professionals should be called on to determine the type of business organization that should be established and to clarify state-specific laws and requirements. Consultants should consider the advantages and disadvantages of each type of organization, evaluate any liability and risk, and consider start-up costs and taxation issues. “Getting Down to Business,” (see below), describes in general terms the different types of business organizations and identifies the advantages and disadvantages of each. It should be noted that not all business organizations described are allowed in every state.

<i>Getting Down to Business</i>		
Business Organization	Advantages	Disadvantages
Sole Proprietorship <i>This type of business has an informal structure. The consultant has complete ownership and control over the business as well as the liability and loss. Income and operating losses can be reported through the consultant's income tax return.</i>	<ul style="list-style-type: none"> • ease of formation • minimal government regulation • low start-up costs • complete ownership • control over all managerial issues • possible tax benefits 	<ul style="list-style-type: none"> • limited capital • limited expertise • limited existence/lack of continuity • limited transferability of the business to others • unlimited liability • image of instability
Corporation <i>A corporation is a legal entity that is separate from the consultant and/or other shareholders. The corporation generates revenue, pays expenses, and generally carries the liability. Articles of incorporation must be filed and fees paid to operate. There are state and federal regulation and taxation issues specific to corporations.</i>	<ul style="list-style-type: none"> • limited liability • access to capital • ease of transferability of shares (with some exceptions) • image of stability • centralization of managerial functions • access to expertise • continuity of existence 	<ul style="list-style-type: none"> • high start-up costs • formalities of formation • extensive government regulation • far-ranging record-keeping responsibilities • double taxation (with certain exceptions—the corporation pays taxes and the shareholders pay taxes on their dividends)
General Partnership <i>Partners enter into an agreement and obtain applicable registrations or licenses to begin operation. Partners have equal share in profits, losses, and liabilities. There is unlimited personal liability even if the liability resulted from actions of another partner.</i>	<ul style="list-style-type: none"> • ease of formation • access to expertise • access to capital • possible tax benefits 	<ul style="list-style-type: none"> • difficulty of transferring ownership • limited existence/lack of continuity • unlimited liability • possibility of forced liquidation
Limited Partnership <i>A limited partnership is more formal than a general partnership but allows more</i>	<ul style="list-style-type: none"> • somewhat greater flexibility than a general partnership 	<ul style="list-style-type: none"> • some rigidity in ownership and decision making • unlimited liability faced by

<i>flexibility. At least one partner must be a limited liability partner. They are only liable for the amount invested in the partnership rather than unlimited personal liability.</i>	offers <ul style="list-style-type: none"> • greater access to expertise • greater access to capital • limited liability 	general partners <ul style="list-style-type: none"> • limited existence • vagaries of controlling state law
Limited Liability Partnership <i>Partners in this organization are liable for their own wrongdoing, but generally not held liable for the wrongdoing of other partners or employees/ agents of the firm.</i>	<ul style="list-style-type: none"> • limited liability for the wrongdoing of others 	<ul style="list-style-type: none"> • unlimited liability for a partner's own wrongdoing and the normal business debts of the partnership • extensive regulation by the state • inapplicability to professionals in some states
Limited Liability Company <i>State law varies for this type of organization. Generally, a limited liability company will file articles for the organization. Individual liability is limited to what is invested in the company.</i>	<ul style="list-style-type: none"> • limited liability for all members • centralization of management 	<ul style="list-style-type: none"> • formalities of formation • extensive regulation by the state • inapplicability to professionals in some states • possibility of federal regulation • uncertainties as to taxation, transferability of shares, duration of the venture, and other issues
Source: <i>Long Term Care Handbook: Resources for the Health Information Manager</i>		

Determining Start-up Costs

An important factor to consider when opening a consulting business is the availability of start-up capital. Most consultants do not have a full client load when starting their business. There is significant lag time between securing the first client, completing the project, billing, and receiving payment. Even if a consultant is lucky enough to have a billable work order completed immediately upon opening, it may still be 90 days before an invoice is paid.

To ensure that there are adequate resources to invest in start-up expenses, a consultant should try to have three to six months of capital set aside to cover operating expenses. Another avenue is to forego a salary or draw a reduced salary to build a financial reserve if it is not possible to start with significant capital. The amount of reserves set aside to cover expenses is based on the salary needs of the consultant and the operating expenses for the business. A common rule of thumb is to have three to six months operating expenses in reserve.

When determining start-up expenses, consider the following:

- salary expectations
- professional fees, including attorney (business organization and contracts), accountant, bookkeeping services, and Web designer as needed
- professional liability or errors and omission insurance
- business cards, letterhead, and other printing expenses
- office expenses, equipment, and utilities
- professional dues, resources, books, and subscriptions
- education and training needs
- personal benefit expenses such as healthcare, disability, life insurance, and retirement

Setting Up an Office

Many consultants who start their own business set up a home office to reduce overhead expenses. Regardless of where the office is located, investment in appropriate equipment and technology will be crucial to running a business and communicating with clients. Below is a list of equipment that is necessary for setting up a functional home office:

- **office furniture**
- **computer**, preferably a laptop. A laptop may be the best investment because it can be used in the office, at the client site, and for presentations
- **computer software**: word processing, spreadsheet, presentation, accounting, and billing software
- **printer, fax machine, scanner, and copier**: the necessity of all four machines will depend on the type of clients and projects. Consider purchasing a machine that combines all four functions as a cost-effective way to have all technology. The scanner and copier are useful in a home office for small copying jobs when corresponding with clients, completing reports, and maintaining business records
- **telephone line and fax line**: a separate telephone line should be dedicated to business. Decide if clients will routinely communicate via fax and if another line is required
- **Internet access**: e-mail account and Web page. Decide between DSL or cable access versus telephone line/modem. Consider the type and size of files sent to and received from clients. If it is necessary to work with large data files, DSL or cable access may be necessary. E-mail is important for networking and communicating with clients as well as professional contacts. A **Web site** is useful in communicating information about a consulting company to prospective clients
- **cell phone or pager**: determine how critical it is to communicate with clients at any time
- **professional resources**: business/ consulting resources (such as books), HIM and other professional resources, current diagnosis and procedure code books or encoders, subscriptions, federal regulations, state regulations, and accreditation standards

Marketing Your Services

Once the decision is made to start a consulting business, an important step in securing the first client is to get the word out and connect with potential clients. The most common ways to communicate include the following:

- **speak** at state, local, or national association meetings and seminars (HIM and other applicable organizations)
- **write** articles for professional or association journals or newsletters
- **tap into** a professional network of colleagues
- **build** new alliances
- **market** services and expertise directly to the client by identifying potential clients and sending solicitation letters
- **become** involved in professional activities to increase name recognition and visibility (including committees, officers, and task forces)
- **advertise** in professional and trade journals or newsletters or association meetings
- **sponsor** a booth or activity at a conference
- **join** a consultants' registry if available
- **create** a Web site with useful information for potential clients
- **develop** marketing materials that include business cards, letterhead, and brochures

Several consultants feel the best marketing tool is "word of mouth," or securing and completing the first project and having satisfied clients tell others about their experience. Many consultants also offer free "value-added services" to their clients to set them apart from the competition. For example, a consultant may develop a client newsletter, offer free client-only seminars, or send e-mail alerts notifying clients of important developments. If a client considers these services to be valuable, they will likely continue their relationship with a consultant and give positive referrals to other potential clients.

Budgeting and Setting Fees

To be a financially successful consultant, fees must be set high enough to cover salary and operating expenses yet be competitive with the market. Because consultants are in the business of selling their time and expertise, they must determine

how many “billable” hours they will have in a year and the rate they will charge. With each client and project, consultants must decide how much of their time they are willing to give away for free and how much will be billed.

Developing a simple budget will provide a financial plan that will help a business succeed. When budgeting for the year, consider the following:

Project yearly income by determining how many hours will be “billable” in a year. New consultants who are used to getting paid for 40 hours of work are often surprised that they work more hours but bring in less income. The key to determining revenue is understanding the balance between billable and non-billable time. A full-time consultant will typically bill between 1,000 to 1,200 hours a year. A consultant running a business must do all the administrative and billing work, write proposals and sell services, attend training and seminars, and take a vacation day or two (all of which is non-billable). Many find that they struggle to get 1,000 billable hours in a year.

Break down billable hour budget and project income on a monthly basis. It is helpful to set a budget for the number of hours that must be billed in a week or month to bring in enough revenue to cover salary and operating expenses. The billable hour target for a week is an estimate—there will be weeks with more hours billed and some with less. Remember to budget for time off.

Formula for determining weekly billable hour target:

$$\frac{\begin{array}{c} \text{\# of billable} \\ \text{hours in a year} \end{array}}{\begin{array}{c} \text{\# of work weeks} \end{array}} = \text{target billable hours per week}$$

$$\begin{array}{c} \text{For example:} \\ 1,000 \\ \text{billable hours} \\ \hline 50 \text{ weeks} \end{array} = 20 \text{ billable hours per week}$$

(Note: Two weeks vacation is budgeted)

Budget expenses throughout the year. Budget routine expenses as well as major expenditures such as seminar, travel, professional dues and resources, taxes, and professional services.

Control the number of projects or clients. It is easy to take on too many projects or clients at one time, which results in work being late or incomplete. Consultants must carefully control the amount of work accepted to assure a quality product is delivered.

Develop fees/hourly rates that cover expenses. The fees charged to a client must cover wages, the additional tax burden, benefits, vacation and sick time, and all operating expenses of the business. For this reason, consultants cannot charge the same rate that they were paid when under employment and expect to make the same amount of money. The hourly rate of a consultant has a direct relationship to the number of billable hours and the salary they would like to draw as a consultant. The following formula will help determine an appropriate hourly billable rate.

Formula for determining billable hour rate:

$$\frac{\text{annual salary}}{\text{billable hours/year}} \times 2.5^* = \text{hourly billable rate}$$

For example:

\$50,000 annual salary $\times 2.5^* = \$125$ per hour

1,000 billable hours/year

**A ratio of 2.5 is common for determining a consultant's billable rate. If overhead expenses are low, a ratio of 2.0 could be used instead of 2.5. If overhead is high, for example due to office rental or administrative staff, a ratio of 3.0 could be used.*

What happens if the hourly rate determined is too high for the market to bear? A consultant can lower his or her salary expectations, increase the number of billable hours in a year, cut operating expenses, or look for other revenue sources to make up for a lower billable rate. Evaluating the professional fees charged can help increase the number of billable hours in a year. It is also important to evaluate the reasonable business expenses charged back to the client.

Determine the professional time charged. The number of billable hours is crucial to the success of a consulting business. Keep in mind that consultants are in the business of selling their time and expertise, so a decision must be made on the professional time that is billed to the client. Following are examples of services that require professional time and should be considered in regards to billing:

- prep time prior to a visit or project
- consultation time at the client site
- report writing time
- telephone consultation time (if charged, often billed in six-minute increments or one-tenth of the hourly rate)
- travel time (if charged, often charged at half the hourly rate for round trip travel)
- research time
- preparation for an in-service or client-specific seminar

The formulas help determine a fiscally sound billable hour rate, but there are other factors to consider when setting fees. The following issues should be considered, and rates should be adjusted accordingly:

- **Fees of existing competition:** It will be difficult to gain clients if you are billing twice as much as the competition. A consultant needs to look at ways to trim the billable hour rate or bring in additional revenue to maintain a viable business
- **Geographic area and practice setting:** Fees will vary depending on the type of consulting work performed, the location, and the practice setting
- **Type of work performed and contract length:** A consultant may price a job lower if taking on an interim management job that guarantees 40 billable hours in a week. Rates for high-volume, long-term clients may be lower than those for one-time limited projects

Selecting Billable Expenses

Consultants often bill expenses related to a consulting project back to the client. When starting a business, determine which expenses will be billed and which will be covered as administrative overhead. The most frequently billed expenses include travel expenses, faxing, copies, long-distance phone charges, and postage and shipping charges.

Some consultants will build an administrative overhead fee into a proposal to cover expenses such as fax, long-distance phone charges, and postage. For example, a fee of one to 4 percent of the professional charges are built into the final proposal to cover non-travel related expenses. Regardless of whether the expenses are billed back to the client, a consultant should maintain a tracking system for tax and budget purposes.

Billing the Client

Consultants typically bill clients monthly, semimonthly, or upon completion of a project, depending on the type of service. It is important to **maintain a schedule or system** for billing to ensure regular income for the business. Keep in mind that many organizations will take between 60 and 90 days to process a payment and issue a check. When finalizing the details of a project or contract, discuss the organization's payable schedule.

Consultants often include a statement in their contract or agreement that the client "agrees to make timely payments." Late fees should be established and charged to encourage timely processing and payment of invoices. If payments are not received, contact the accounts payable clerk at the organization to determine if the invoice was received and when it will be paid.

The content of the invoice may vary based on the type of project. Generally, professional services are separated from billable expenses. For consultants billing by the hour, clients typically like to see the breakdown of hours and activities performed. The content of the bill and breakdown of charges typically matches the proposal and pricing of a project.

Identifying Other Revenue Sources

Consultants often search for other means to generate revenue for their business. They may sponsor and conduct seminars or create and publish manuals, books, resources, and newsletters to bring in other sources of revenue.

Understanding Tax Implications and Accounting Records

As a general rule, an independent consultant generally pays higher taxes than someone who is an employee of a company, depending on how the consulting business is organized. For example, a sole proprietor will pay income taxes in his or her applicable tax bracket (28 percent) plus the full social security tax of both the individual and employer contribution (more than 15 percent). A consultant could pay more than 40 percent of his or her income in federal taxes plus applicable state taxes. Not all revenue generated by a business is taxed. Business expenses are deducted first and taxes are applied to the remaining profits. It is important to work with an accountant to set up the best tax strategy, develop a business record keeping system, and file applicable income tax forms including quarterly estimated taxes.

Consultants often invest in accounting software to assist with bookkeeping such as accounts payable, accounts receivable, and expense tracking. Many will purchase the software recommended by their accountants. Consultants who do not have a background in running a business should consider taking a class in small business administration.

Tracking expenses and keeping receipts is critical. Accountants can assist with identifying the expenses that must be tracked and discuss strategies such as home office deductions and business use of a vehicle. Unless a vehicle is owned by and used solely for a business, maintain a log of mileage to allocate between personal and business use of a car. When mileage is charged back to the client, keep a record of the exact mileage and dates. When traveling to a client site, retain all receipts: meals, hotel, car rental/taxi, airfare, parking, tips, and other incidentals. A simple method to manage receipts is to use an envelope for each business trip to track and retain receipts and aid in record keeping upon return.

Writing a Proposal and Pricing a Project

One of the most challenging steps in securing a new client is developing a proposal that accurately identifies the needs of the client, addresses the key areas of a project, communicates the consultant's approach, and accurately estimates professional time and expenses. Unfortunately, there is not a formula for writing a winning proposal, but there are common characteristics. The proposal should outline the problem, steps, timetable, solution, and costs/budget.

Pricing a project is often difficult and subjective because fees may fluctuate based on market pressure and negotiations. There are a variety of acceptable ways to price a project. Often the type of project, type of consulting services, geographic area, or practice setting will drive the pricing. The following list provides examples of how projects or services can be priced:

- **Per hour:** charge the billable rate for all professional time provided to the client. Some consultants charge a high hourly rate (e.g., two times billable rate) for on-site consultation time only that includes travel, report, and telephone consultation time
- **Per day:** charge a flat fee per day on-site that includes all professional time for a project
- **Per project:** develop a price for an entire project or per phase of a project without a breakdown of professional time

- **Per chart coded or per audit:** in some areas of practice, clients prefer to pay by chart because it guarantees a level of performance. Consultants should have an understanding of the average time to code or complete an audit to determine an appropriate fee per chart
- **Retainer:** the client agrees to pay a monthly or annual retainer to guarantee access to a consultant's services or advice
- **Interim management or fill-in:** special pricing may be established for staff replacement. The professional fees are usually lower because there is a higher number of billable hours guaranteed
- **Fees per in-service or education programs:** develop special fees for providing client-specific training. Charging the hourly billable rate for a one-hour in-service may not be sufficient to capture preparation and travel time

Depending on the project, it may be necessary to have part of the professional fees paid up front. For example, if the project requires significant prep time or review of organization policies, documents, or cases before an on-site visit, a consultant can negotiate with the client to have a portion of the fees paid up front.

Developing Contracts and Letters of Agreement

Typically a contract or letter of agreement (engagement letter) is signed by both the consultant and the client to protect both parties by formally acknowledging the relationship, clearly stating the deliverables of a project or scope of services, and detailing the fees and expenses charged. HIM consultants should determine if they are a business associate when working with a healthcare provider, payer, or plan that is covered by HIPAA. If so, the contract or letter of agreement must contain required business associate language.

A contract is often used when consulting services are provided on a long-term basis. The contract outlines the scope of services provided and the fees and expenses to be paid by the client. Contracts are often updated and re-signed on an annual basis. This gives the consultant the opportunity to adjust fees as necessary.

A letter of agreement rather than a contract is typically used for projects rather than on-going consultation services. Engagement letters typically include the deliverables of the project and fees to be paid. The letter is written and signed by the consultant with the client signing and dating the letter to acknowledge acceptance of the engagement.²

Writing a Report of Consultation

A report of findings from a consultation visit or a summary of the project is typically written to provide the client with documentation. The following types of information are commonly found in consultation reports (the exact content and format will vary based on the project or services):

- date of visit (or date range of project)
- objectives
- findings, observations, or progress
- recommendations
- conclusion
- consultant's signature

(Note: if chart audits are conducted and findings must be reported, do not include patient names in the report)

The report should be sent to the individual who contracted the services and anyone he or she has designated to receive a copy. If the consultant is working through an attorney, a statement titled "attorney work product" should be printed on each page. When working with an attorney, consultants should follow their guidelines for documenting findings. Many consultants include the following statement to keep their findings from being used against a facility during a department of health survey or litigation if applicable: "Facility XYZ Quality Assurance Committee work product. Any reports shall be part of the facility quality assurance documents and considered confidential."

Reports should be completed in a timely manner after completion of a consulting visit or project. A good rule of thumb is to have the report completed no later than 10 working days after completion of a consulting visit.

Hiring Staff

Hiring additional professional staff or administrative support has significant implications for a consulting business. Work with an accountant to determine the payroll, benefit, and tax issues. Also consider the overhead expenses involved with hiring staff.

An alternative to hiring staff is to subcontract with other professionals to complete projects or take on new clients. The consultants would be independent contractors working under your direction in a project. Determine the fees paid to the subcontractors and when they will be paid. Usually the amount charged to the client covers the subcontractors' hourly fees with an add-on for administrative expenses. Determine when the subcontractors will be paid—upon completion of the project regardless of when the consultant is paid or only when the client has paid for their services.

The opportunities are endless for consultants in the HIM profession. Continuous changes in regulations, reimbursement, and automation provide new avenues for professional services and expertise. Starting a consulting business with the proper foundation promises long-term viability, prosperity, and success.

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Notes

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2. Hughes, Gwen. "Practice Brief: Letters of Agreement/Contracts (Updated)." *Journal of AHIMA* 72, no. 6 (2001): 64G-64I. Available at www.ahima.org/journal/pb.html.

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Acknowledgments

Donna Didier, RHIA, CCS
Kathleen Frawley, JD, MS, RHIA
Gwen Hughes, RHIA
Rita Schichilone, MHSA, RHIA, CCS, CCS-P
Mary Stanfill, RHIA, CCS-P

Article citation:

Dougherty, Michelle. "Starting a Consulting Business (AHIMA Practice Brief)." *Journal of AHIMA* 73, no.5 (2002): 56A-G.

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