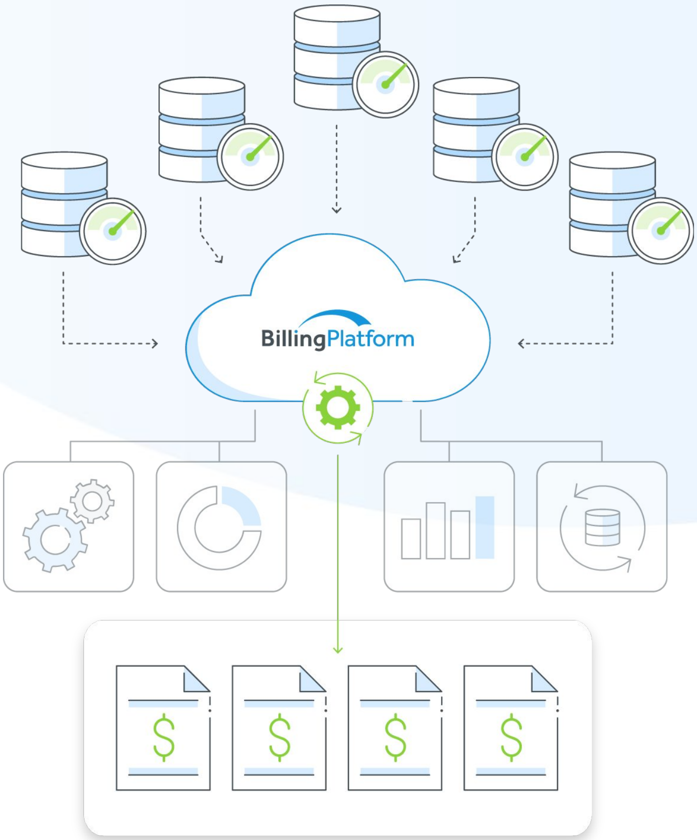
WHITEPAPER

Usage-based Billing - Is it Right for Your Business



Driven by the continued shift from on-premises license software to software-as-a-service (SaaS) models, in conjunction with the increased need for new software collaboration tools during COVID-19, [the SaaS market is forecast to grow to $141 billion by 2022](). With a delivery model that is scalable, easy to use, cost-efficient and quick to deploy, it's clear why this business model is predicted to grow over the coming years.

However, along with growth comes new market entrants, increasing the number of competitors you need to rise above. As with any business, your pricing model has a direct effect on your profitability. For SaaS companies, getting your pricing strategy right is even more critical.

SaaS pricing models rely on your offering's perceived value, and that means striking the right balance between your offering's value and its price.

Differentiate with Pricing Innovation

Regardless of the pricing model SaaS businesses deploy, you'll find varying degrees of complexity, functionality and innovation. Companies that understand the need for a tactical approach to their pricing strategy will use these aspects to differentiate themselves from their competitors.

From basic models such as flat-rate to more complex models like hybrid (and everything in between), you have countless options to choose from. However, determining the right one that'll optimize your pricing strategy can be tricky.

SaaS Pricing Models: Are You Charging Enough?

With so many pricing models to choose from, it's easy to become overwhelmed. To help you find your pricing strategy sweet spot, we've reviewed the most prevalent SaaS pricing models.

We've highlighted their pros and cons, and provided examples of businesses that are successfully using each of these strategies.

Flat-rate Subscription SaaS Pricing

Frequently used in the early days of cloud computing, this pricing model enables SaaS businesses to charge customers fixed, recurring fees for access to products and services. Payments for flat-rate pricing are usually collected monthly or annually.

Example: A B2B and B2C company, Adobe Creative Cloud provides a variety of applications for individuals, businesses, students and teachers, and schools and universities. Depending on the target market and the application, their prices range widely to fit consumers' needs, but are typically fixed per segment.

Pros: Easy to understand and sell, subscriptions are typically evergreen contracts, meaning they auto-renew each billing cycle – providing SaaS businesses with a predictable revenue stream.

Cons: Customers can cancel their subscriptions at any time, and pricing isn't directly tied to utilization. In addition, customers who want more flexibility may find flat-rate subscriptions too constraining.

Usage-Based SaaS Pricing

SaaS businesses that need more advanced billing capabilities are gravitating towards usage-based (pay-as-you-go) pricing that scales with utilization. Oftentimes usage, or "consumption-based", pricing sits on top of recurring subscriptions.

Example: With countless product categories, Amazon Web Services (AWS) provides customers with over 160 cloud services at varying tiers. There's even a free tier that contains over 90 products and services. Customers only pay for services consumed, with certain cloud services such as those that handle micro-processes incurring a per second charge.

Pros: This billing strategy provides greater flexibility to customers since they can link consumption to a variety of activities. With usage-based SaaS pricing models, companies charge users based on resources consumed, time spent using services, the number of events triggered, and more. Essentially, customers who use more resources are charged more.

Cons: Although a straightforward pricing model, revenues can be hard to predict, as usage can fluctuate from month to month.

Tiered SaaS Pricing

A popular and flexible pricing model, SaaS companies are able to offer multiple packages at different price points. Packages can differ depending on the features, widgets, or activity thresholds they include.

Example: Zendesk, a provider of customer relationship management (CRM) solutions, provides support, sales and platform options. Within each of these applications they offer 2 – 3 pricing tiers. For example, there are 3 support pricing tiers starting at $5/agent; their sales suite provides 2 options, starting at $19/seat; and they offer 3 platform choices with Lite at no charge, Professional at $19 per agent/per month, and Enterprise at $59 per agent/per month.

Pros: Provides SaaS businesses with the ability to target their offering to specific buyer personas and upsell to existing customers. This pricing model makes it easy for customers to know exactly what they'll receive at each tier.

Cons: Customers can become overwhelmed and not understand their choices if presented with too many pricing options. For this reason, it's recommended that you create only 2 – 4 tiers per offering.

Per-User SaaS Pricing

For many SaaS businesses, it makes sense to charge clients based on how many users or seats they need. Under these pricing arrangements, customers pay a fixed monthly or annual fee for access to a predetermined set of features and functionality.

Example: With 15 application options, Salesforce provides different editions with varying features within each of their solutions. Prices range from $25 per user/per month to over $300 per user/per month. This enables them to target businesses of all sizes.

Pros: With this fixed pricing model, revenue is highly predictable. To make the option more attractive, some SaaS companies deploy variations on this pricing model. Some offer per-user prices by tiers, and others only charge for active users. The latter strategy is better suited for larger enterprises that may not always know the exact number of users who need access to a given service or platform.

Cons: A one-size-fits all approach to pricing, it's becoming dated given the way customers now use applications. In addition, you may lose revenue if login details are shared among employees, instead of the company purchasing additional licenses.

Per-Storage SaaS Pricing

The cloud storage market has grown rapidly in recent years. Therefore, per-storage SaaS pricing models are a direct result of this trend. SaaS companies in this sector charge individuals or businesses based on how much digital space they need.

Example: Dropbox lets users store up to 2 GBs worth of data for free, which is plenty for most individuals. Beyond that, the company charges $9.99 per month for up to 2 TBs of storage, and $16.58 per month for up to 3 TBs of storage. Within each of these options they provide various storage and access functionality.

Pros: To make their offering attractive to users, many cloud storage sellers offer space for free up to a certain amount. Once the limit is reached the customer is charged based on various tiers.

Cons: With this pricing model, cloud storage sellers may incur IT maintenance and management expenses for a large proportion of users who aren't generating revenue.

A La Carte SaaS Pricing

Some SaaS providers now offer customers the ability to pick and choose which features they want and need. Accomplished through eCommerce-style shopping interfaces, users add individually priced features to their carts, and are charged on a recurring basis.

Example: From free tools to a variety of CRM applications, HubSpot gives customers product and plan options, as well as bundles. The company's interface is easy to use, and customers can see their final monthly payment listed by feature.

Pros: From a customer perspective, they only pay for the features and functionality needed. By enabling customers to choose what they want, SaaS businesses gain tremendous insight into what their users value.

Cons: This pricing tactic makes it difficult for customers to make accurate comparisons across different providers. Especially if only one offers a la carte options. It's also one of the more complex SaaS pricing models for companies to manage.

Hybrid SaaS Pricing

Increasingly, SaaS companies are deploying hybrid pricing models that combine multiple tactics. One of the most powerful combinations is a flat-rate plus usage-based pricing model that gives users both pricing and feature flexibility. Alternatively, some SaaS companies offer the subscription/usage combination within different pricing tiers, and then include an a la carte component for add-ons.

Example: Zoom uses hybrid pricing to give customers options around how they use and pay for platform access. The company offers four different pricing tiers, each with its own set of add-ons and usage rates.

Pros: This pricing model provides SaaS businesses with countless opportunities to upsell customers in addition to recurring cash flows.

Cons: Hybrid pricing can get very complicated, very quickly. SaaS businesses must have a powerful billing solution to efficiently manage these pricing tactics at scale.

Deploy Any Combination of SaaS Pricing Models With BillingPlatform

To optimize your revenue potential, you need a sophisticated, cloud-based billing solution that gives your pricing team the functionality they need to differentiate your offerings through flat-rate, consumption-based or a hybrid approach. With BillingPlatform, not only can you support those models, but with our innovative pricing strategies, you can go a step further.

For example, using workflow automation and mediation, you can create hybrid models with consumption-based pricing elements. Alternatively, you can fluctuate price based on demand, such as when the price for an airline seat goes up when availability decreases. Contact our team today to learn more about how BillingPlatform can help accelerate your business growth!