The definitive guide to feature-based pricing

Booklet

Binary Stream

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Introduction to feature-based pricing

Feature-based pricing is one of the leading SaaS billing models, allowing companies to price their services and products based on varying levels of functionality. It's most commonly paired with a tiered pricing strategy, where access to more features increases the price.

Although considered an innovative strategy by many, feature-based pricing is not a revolutionary concept and has a lot in common with more traditional pricing. If you think about most services and products you pay for, you will find that a higher price usually means more features. Consider any item you can purchase, and you will begin to see that features almost always play a role in the cost.

Here are just a few examples of everyday feature-based pricing:

- Gym memberships charge extra for features such as a personal trainer, access to saunas, or even a diet plan.
- Magazine subscriptions cost more for features such as archive access, print and digital copies, or discounts on related publications or services.
- Premium coffee machines offer extra features like milk frothers, customizable settings, or multiple grinder settings.
- Laptops increase in cost based on additional storage, faster processor speed, and extended battery life.

Feature-based pricing is not a revolutionary concept.

Even though this pricing model is easy to understand, it's not necessarily straightforward to implement. You will need to consider how to use this strategy to the best effect. This booklet offers a guide to the pros and cons and a breakdown of different approaches to pricing per feature.

A quick glance at the pros and cons of feature-based pricing

- Customers understand pricing growth
- Upselling is more natural
- Option to trial basic features
- Works well with other models
- Easy to set user expectations
- Allows for resource segmentation
- Appropriately charge for complexity

- Managing upgrades may be tricky
- Balancing your basic plan
- Developing unnecessary features
- Choices can confuse customers
- Customers feel locked out
- Difficult to segment features

Understanding the pros of feature-based pricing

Customers understand feature-based pricing strategies

Usually customers know why they're paying more. It can also make it easier to scale their usage, with customers levelling up when they require more features. Although, it's worth noting that this will require flexibility and the ability for easy upgrades.

Upselling is more natural

When they first sign up, many will choose a cheaper option with fewer features. Once customers are happy with their subscription, you can build on their package by suggesting upgrades where you see a need for some of the premium features. You will likely see customers upgrading without any encouragement if they begin to require additional functionality.

Easily set up an option to trial basic features

Particularly in the SaaS world, it's common for customers to pay an entry-level fee for a more basic subscription. Often these are designed with the cautious customer in mind, allowing them access to some of your best-loved features, but limiting the usage of the functionality.

It works well with other pricing models

Companies can reap even more benefits by strategically pairing it with a hybrid of tiered, bundling, or usage-based pricing (or a combination of one or more of these models).

Easy to set customer expectations sales of certain products

Customers pay only for the features they are interested in, and your service/product specs will define what users have access to at each price point. Because you break down your offering by features, customers are less likely to be confused about functionality as they will have chosen a payment plan based on it. Of course, this also depends on your ability to communicate what features are available at different costs effectively.

Allows for better segmentation of your resources

Segmentation can give you more accurate performance metrics based on the features customers use. It's often the case that some features require a lot more work on your end to deliver. Suppose you've 500 customers using your essential features and only ten using your premium features. Depending on how much extra you charge for premium functionality, committing too many resources to those contracts may not make sense. You can use segmentation to support the core revenue stream.

Appropriately charge for complexity

With this pricing model, you can lock functionality that is expensive to maintain or requires a lot of training, making it part of your premium package. Those that want to use these extra features can upgrade, and you do not have to lose revenue by operating expensive services at lower price points. A core benefit, particularly if you consider flat-rate pricing strategies where all customers would have access to costly features regardless of usage.

Understanding the cons of feature-based pricing

Managing upgrades may be tricky

One of the keys to success in implementing feature-based pricing is the ease with which customers can upgrade. It's worth noting that if those who buy a cheaper model cannot upgrade effortlessly, they may end up having to purchase other services elsewhere. If you fail to account for the possibility of changes to subscriptions, you're creating a poor customer experience. Whatever you're selling, upgrades must be straightforward so that customers can access premium features without jumping through hoops.

Balancing your basic plan may present difficulties

It's not always possible to offer your premium functionality at lower price points. However, the functionality must still be attractive enough so that you can gain and retain customers. Sometimes implementing limited usage of top features on the basic plan can be an answer to this dilemma.

Developing unnecessary features that end up costing too much to run

To sell upper tiers, teams can become distracted by offering infinite upgrades and spending a lot of time and energy creating new and exciting functionality. It's worth segmenting your resources based on revenue streams to prevent this from happening.

Choices can confuse customers

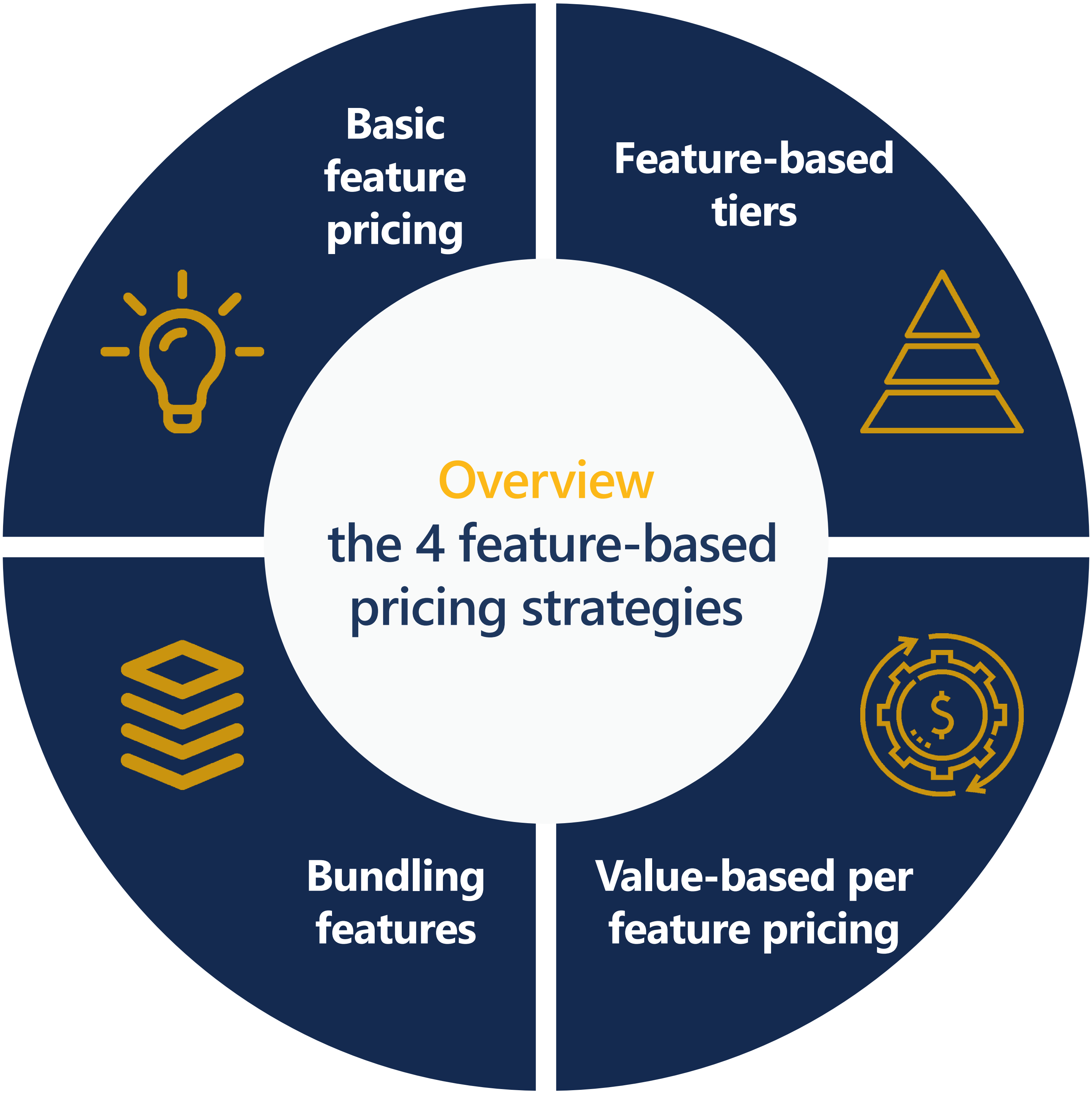
Customers may feel overwhelmed by too many options and struggle to understand too many features. If you stack higher tiers with excess functionality, it may not always align with a customer’s wants and lead to decision paralysis.

Customers feel locked out of premium features and resentment can build

At your lower levels, ensure enough functionality to solve some of your customer’s core problems.

Difficult to segment features into different packages

Segmenting features into tiers may be tricky, and you could lose some of your perceived value; an issue prevalent in situations where premium features are used in marketing as lead magnets yet are not available in lower or mid-priced tiers.


Basic feature pricing
Feature-based tiers
Overview
the 4 feature-based pricing strategies
Bundling features
Value-based per feature pricing

Basic feature pricing (with example)

Even basic feature pricing tends to use tiers to segment each subscription level. Companies will usually divide their features into three price points, each allowing users slightly more access. What happens in the most stripped-back version is that the bottom tier will often be the stickiest, offering the most features and perceived value to potential subscribers.

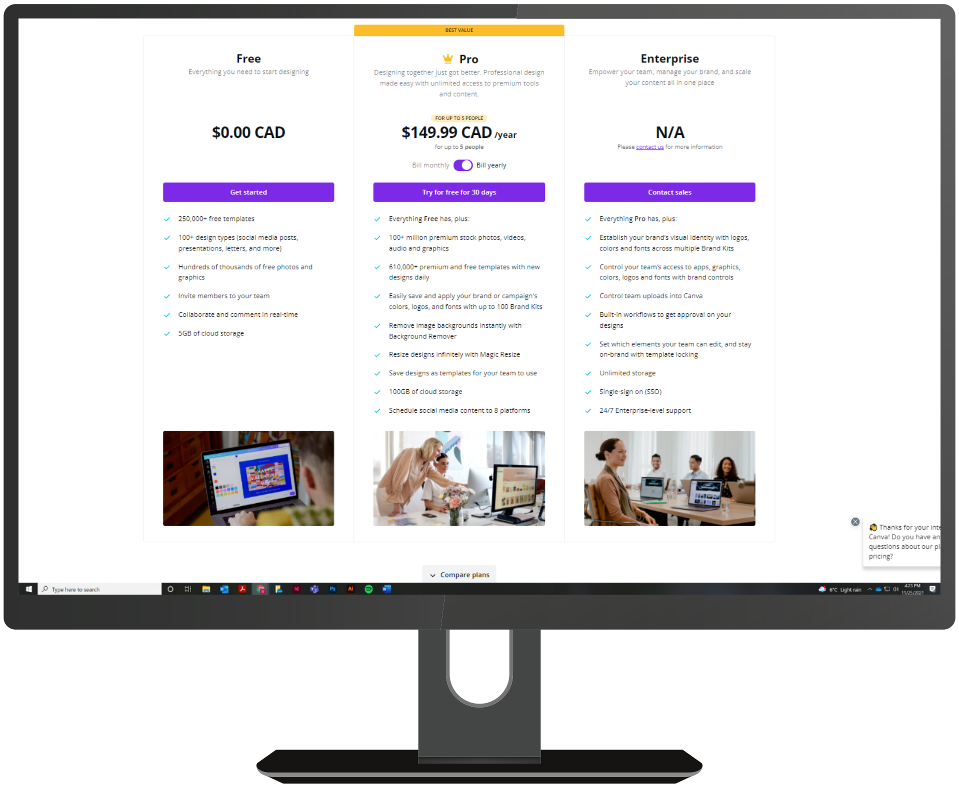
The Globe and Mail is an example where it is cost-effective for the newspaper to prioritize selling digital access. Although you can pay more to receive print copies, the higher tiers offer no other extra features, with the most expensive subscription simply supplying print versions on a greater number of days. This approach makes print delivery a luxury and incentivizes subscribers to choose a digital subscription. An effective strategy, given the high cost of printing and the supply chain issues involved when delivering physical papers.

Feature-based tiers (with example)

Feature-based tiers can take many forms, and most businesses will use some combination of tiered pricing strategies to sell products/services. The lowest or cheapest tiers are usually entry-level lead magnets, inviting potential subscribers to trial features for free or at a minimal cost. Higher tiers will often load each price point with impressive features and employ psychological pricing tricks like anchoring and price skimming.

Canva is a graphic design tool that has mastered the art of feature-based tiers. The lowest subscription level offers access to a wide range of attractive features, allowing subscribers to trial the product with a low barrier to entry. This is also a freemium strategy, allowing users to sign up with an email and explore the design tools.

For this to work, you must be very confident in the attractiveness of your higher tiers and have a high percentage of upgrades once subscribers trial the lower levels. If you look at the landing page below, it's also clear that the "preferred option" is pro. Free users are continually reminded of pro features when designing, making the idea of upgrading a constant choice as they navigate their options.

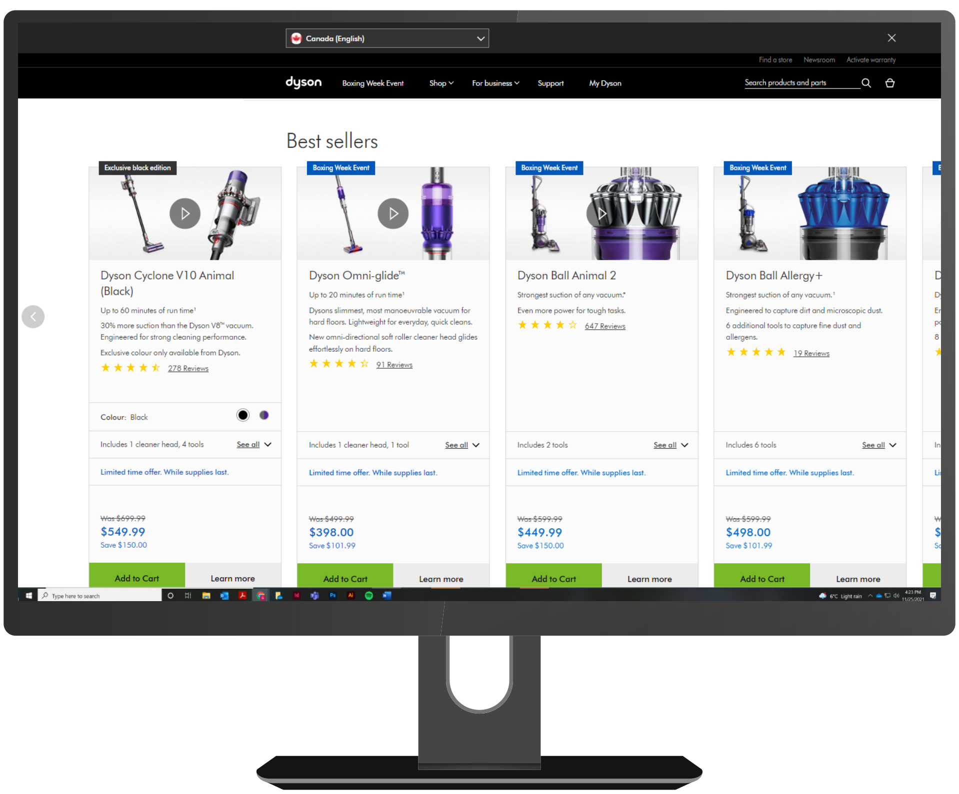


Value-based per feature pricing (with example)

Value-based pricing coupled with per feature pricing can be an extremely effective strategy. It allows you to charge based on the perceived value of your features rather than the exact cost of developing them. Its success depends on meticulous market research and a solid understanding of your features' worth to your target audiences. Established brands often use it as they can bank on awareness of their reputation to charge premium rates.

One of the keys to getting value-based pricing right is understanding differentiated worth, i.e. knowing which unique features set your product apart from the competition. This information will allow you to determine the perceived value of that difference and create pricing that takes advantage of your strengths.

Dyson is an established brand that sells vacuums using value-based per-feature pricing. Their pricing pages present different price points on a sliding scale—vacuums have lower functionality at lower prices. The key features are immediately apparent, and the copy even compares each vacuum's suction to one of Dyson's legacy products. This tactic only works because the core audience understands the reference, and it helps them to distinguish between prices.

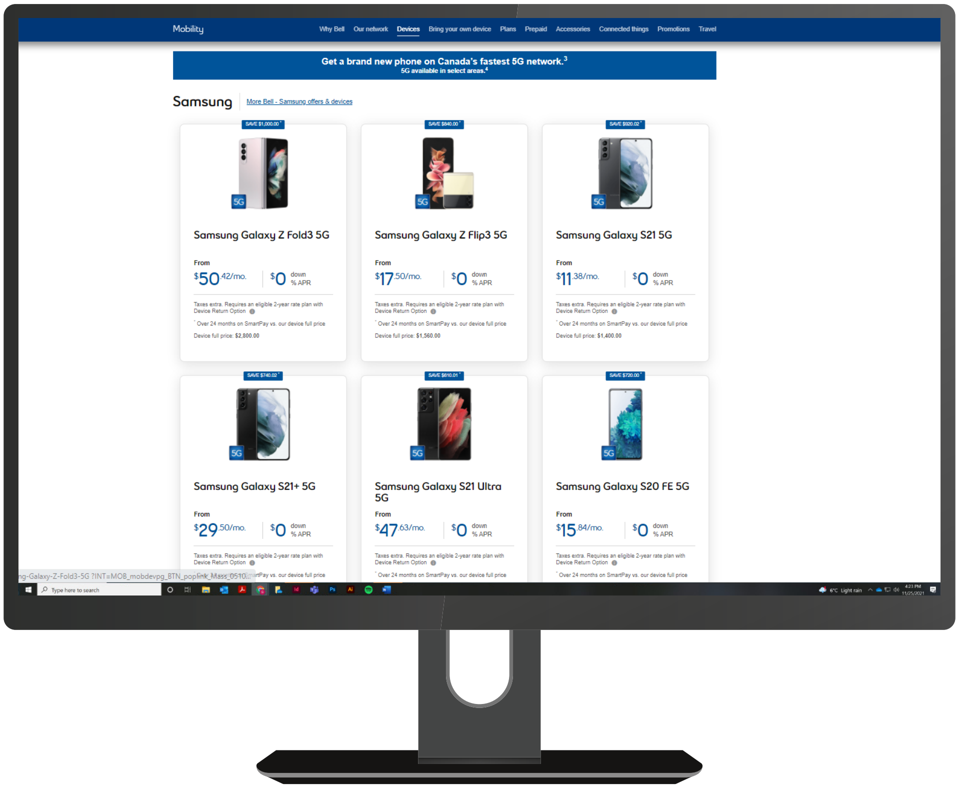


Bundling features (with example)

Standard across all industries, bundling is an age-old technique for selling a group of products or services. The main appeal for companies is the ability to make products or services more attractive by selling them in sets. It is critical to understand what elements of your product/service will incentivize sales and use these features to help differentiate between various bundles.

Phone companies are strong examples of bundling features, often using a new phone or device bundled with a data package to sell their service. It is mutually beneficial because the customer gets the phone they want at a reduced rate, and the phone company sells a lot more than just the phone.

Bell's Samsung Galaxy pricing is an example of this. Customers pay nothing for the phone upfront, and instead, they sign up for a 2-year phone plan and buy the phone at a reduced rate charged in installments in their monthly phone bill. New devices with the flashiest features are the big selling point, but the real aim is to bundle these phones with more lucrative features such as data, minutes, and international calls.



A short guide to revenue recognition for feature-based billing

Managing revenue recognition and deferred revenue for featured billing depends on how and when customers pay for your product/services. If they pay a monthly fee, it's possible to recognize that revenue each month when earned. However, it's not quite as simple for those paying an annual subscription. Rather than recognizing revenue immediately, you will need to set up a deferral schedule and only recognize revenue when earned over the year. The easiest way to do this is to divide it into monthly installments.

Revenue allocation is one of the core ways companies can understand the profitability of their features.

Revenue allocation is one of the core ways companies can understand the profitability of their features. Each component earns a certain amount of revenue, and accurately allocating revenue to features is critical. For instance, if you're selling websites to companies at various price points, with your most advanced option costing 25,000 CAD and your least expensive costing 5,000 CAD. You must break down the features of each level and perform a comprehensive margin analysis to see where your revenue is coming from and to understand what features are high-earners worth further development. You may also notice features that are a drain on resources.

The complexity of managing subscription billing models is introduced by the wide range of options available to customers (do they want annually, monthly or quarterly billing?). Most companies will require a robust billing solution in place to handle this as they scale. A solution should streamline complex billing and also automate revenue recognition and deferrals to allow you to remain compliant with accounting standards like ASC 606 and IFRS 15.

Managing the complexity of feature-based pricing

It perhaps comes as no surprise that companies will not implement feature-based billing without careful consideration. Below is a short guide to help you understand the critical components to a successful implementation.

The 3 critical elements of your feature-based pricing strategy

1. Expand your understanding of your features

Companies are often so distracted by the critical features of their software or product that they forget about their people. Both are important. Take time in the early stages of your pricing strategy implementation to define every single feature your company has to offer and understand the perceived value of each one. It can be a surprising exercise and reveal differentiators that will help set your various price points apart.

2. Combine with other pricing strategies

It's hard to implement effective feature-based pricing without embracing a hybrid model. As discussed earlier in this article, it combines well with several approaches. Consider the models that make the most sense for your features, and develop a strategy that will make the most sense for your audience.

3. Manage revenue allocation and deferrals

Automating revenue recognition and understanding the complexity of allocating revenue to features will be critical for high performance. Investing in a robust billing solution will allow you to do this at scale and provide you with the tools to get accurate insights when performing margin analysis on your features.

Introducing Subscription Billing Suite

A comprehensive solution for billing, deferrals, and recognition that streamlines the entire quote to cash process at every step from billing and invoicing to reporting and forecasting. It provides consistent and reliable invoicing for a wide range of pricing models and allows you to take control of your pricing and billing schedules at the line-item level within Microsoft Dynamics 365 for Finance and Operations, Microsoft Dynamics 365 Business Central, and Microsoft Dynamics GP.

What our customers say

> Wonderful, wonderful, wonderful. A joy to work with Binary Stream. Everyone was super helpful and positive, which had a big impact on the success of the implementation.

MoxiWorks

> What makes Binary Stream different from other software companies we have worked with is their ability to truly listen to customer input and enhance their subscription solution to meet those needs.

ibexa

> Since I have come on board, Subscription Billing Suite has paid for itself more than once over. Having this solution to help us manage over 10,000 deferred contracts is an essential part of our financial processing.

BT

> I've long been a fan of Dynamics, and Subscription Billing Suite met and exceeded every feature of our previous solution. However, the factor that made this project a success is having a partner who augmented our internal integration efforts.

OTC Markets

Binary Stream

Start your financial transformation journey today

Learn more by reading our complete guide to subscription management, offering insights into billing models, pricing page psychology, and plenty more.

Discover more