Mastering Hybrid Pricing: Usage-Based Billing + Subscriptions = The Future

Best practices to implement hybrid and usage-based billing with predictability for subscription companies.

Introduction

Hybrid and Usage-Based Billing for Subscriptions

In the era of algorithms, simple subscription billing alone is no longer enough. The future lies in hybrid pricing, combining usage-based and annual contract pricing to offer flexibility and agility, essential for customer satisfaction and competitive advantage.

The rise of AI is driving the need for greater flexibility in pricing. In a recent McKinsey study, 65 percent of organizations said they regularly use Gen AI in at least one business function, up from one-third last year. Adopting usage-based billing can increase the appeal of AI companies by providing pricing tailored to customer behavior and resource consumption.

In addition, the current economic landscape, marked by rising interest rates and inflation, has prompted customers to adopt more reasonable spending habits. They often favor paying based on actual usage rather than committing to rigid multi-year contracts that fail to align with their consumption patterns. As a result, procurement teams are advocating for usage-based pricing (UBP) or usage-based billing (UBB) in contractual agreements.

Whether you're an agile start-up or a global enterprise, integrating usage-based billing components into your pricing is no longer just an option—it's a solid strategy to future-proof your revenue. This guide explores the current and future potential of usage-based billing, offering insights into leveraging this flexible pricing strategy to increase customer lifetime value and drive sustainable growth.

Chapter 1: Understanding Usage-Based Billing

What is usage-based billing (UBB)?

Usage-based billing (UBB), or metered pricing, represents a shift in how you monetize your offerings. Unlike traditional fixed-rate subscriptions, where customers pay a flat fee regardless of usage, UBB adapts pricing according to the actual consumption or usage of the service or product. This approach aligns costs more closely with the value delivered, offering flexibility and potential cost savings for customers while providing a scalable revenue stream.

Key differences between usage-based billing and traditional billing models

The main distinction between UBB and traditional billing lies in the granularity of charges. Traditional models often involve fixed monthly or annual fees, providing customers with predictable costs but potentially overcharging or undercharging based on actual usage.

In contrast, fully UBB introduces a variable pricing structure where costs directly correlate with usage metrics such as data consumption, API calls, active users, or transaction volumes. This approach improves transparency and enables you to tailor pricing more precisely to customer needs and behavior, fostering a deeper sense of value and satisfaction.

Hybrid pricing represents a distinctive model that combines fixed-rate structures with usage-based components.

Industries and companies using usage-based billing successfully

Usage-based billing (UBB) has gained significant traction across a variety of industries, fundamentally reinventing how companies engage with their customers and optimize revenue streams.

Leading technology companies like Amazon Web Services (AWS) introduced components of UBB pricing by charging customers based on compute hours, storage usage, and data transfer, effectively aligning costs with actual usage. Telecommunications providers like Verizon have also adopted a hybrid pricing approach, charging for data usage, voice calls, and SMS messages while offering tiered pricing that scales with consumer demand.

Software-as-a-service (SaaS) companies such as Salesforce and Zendesk have integrated UBB components to offer flexible subscription tiers based on active users or feature usage, accommodating diverse customer needs while maximizing revenue. Notably, GenAI companies like Jasper and DeepL leverage UBB as a critical aspect of their pricing strategy, allowing users to pay based on their consumption of AI capabilities and increase customer satisfaction through personalized pricing.

Additionally, AI-enabled software firms, such as those employing conversational agents like Intercom's AI, have explored outcome-based pricing models. These models link pricing to the value delivered, creating a compelling proposition for customers who prefer to pay based on results achieved rather than fixed fees.

Beyond technology, industries ranging from utilities and healthcare to automotive and entertainment are increasingly exploring UBB to innovate pricing models and increase customer engagement. As these diverse sectors adopt hybrid pricing strategies that blend UBB with traditional models, the future points toward a more adaptable and customer-centric approach to pricing in subscription businesses.

Chapter 2: Key Components of Usage-Based Billing

Consumption Tracking/Metering: Tracking usage accurately

Metering forms the foundational element of UBB, involving measuring and tracking customer usage metrics. This process typically encompasses monitoring activities such as data consumption, service usage duration, API calls, or any other relevant unit of measurement specific to the product or service offered. Advanced metering systems integrate with applications and platforms to capture real-time usage data, ensuring accuracy and reliability. By tracking usage metrics, you can provide transparent billing based on customer interactions, increasing trust and accountability.

Aggregation: Calculating cumulative usage for billing

After gathering usage data through metering, the next step is aggregation. This process consolidates and computes the accumulated usage data over the billing period to determine the final value used for pricing subscription services. Aggregation involves compiling metered data, standardizing units of measurement if necessary, and summarizing usage records into larger periods like hourly or monthly totals. Aggregation could also be any function: sum(total), count (number of usages), minimum, maximum, etc.

Defined aggregation rules ensure accurate calculation, including handling overlapping usage periods and applying discounts specified in the billing agreement. Once aggregated, this data forms the basis for computing the total volume of resources or services subscribers consume. It's crucial to bill customers accurately based on their actual usage.

Rating: Assigning prices to measured usage

Once usage data is calculated through aggregation, the next important component is rating or applying pricing rules to the measured usage. Rating engines or systems evaluate the accumulated usage data against predefined pricing structures, determining the applicable charges for customers. Rating involves configuring rate plans, defining pricing tiers, and applying discounts or promotions based on usage thresholds or customer segments. Effective rating mechanisms enable you to align pricing dynamically with customer behavior and market demands, optimizing revenue while offering flexible options to customers.

Billing: Generating invoices based on usage data

While rating computes the charges for a particular usage line item, billing brings together all the line items - usage and non-usage, as well as taxes— into a single compliant document for invoicing and payment collection.

Billing in the context of UBB involves generating accurate invoices that reflect the dynamically calculated charges based on measured usage. This process integrates metered data and rated pricing to produce detailed billing statements that outline the services consumed and associated costs. Automated billing systems, like Chargebee, streamline invoicing processes, handle complex calculations, and ensure compliance with regulatory requirements. Specifically, this is where taxes are applied on the final charges based on your and your customer's region, the type of products, etc.

You can increase customer satisfaction and facilitate efficient financial management by delivering clear, itemized invoices. In addition, robust billing capabilities support revenue recognition and financial reporting, providing deep insights into revenue streams and customer profitability.

Chapter 3: Implementing Usage-Based Billing Components

Implementing usage-based billing (UBB) components involves several key considerations and challenges you should actively address to transition successfully to this dynamic pricing model.

Preparing your subscription model for usage-based billing

Preparing your subscription model for UBB requires a strategic approach to align pricing with customer usage patterns and business objectives. Key pain points include testing new pricing models and gaining visibility into margins.

Choosing the right metering methods and technologies

Appropriate metering methods and technologies are critical to accurately capturing and measuring customer usage. Based on the nature of your services and customer interactions, you should consider options such as event-based metering, time-based metering, or hybrid approaches. Advanced metering technologies integrate seamlessly with applications and IoT devices, ensuring real-time data collection and improving billing accuracy.

Understanding different metering methods: Event-Based, Time-Based, and Hybrid Metering

Implementing usage-based billing components in subscription businesses requires a clear understanding of different metering methods. Here's a quick overview of three common approaches: event-based, time-based, and hybrid metering.

Event-based Metering

Charge customers based on specific actions or events they trigger within your service.

Example: A cloud storage service charges users for each file upload, download, or API call within a billing cycle.

Benefits:

- Clear billing based on actual usage

- Costs align with the value received

- Easy to implement for well-defined actions

Time-based Metering

Bills customers according to the duration of service use.

Example: A video conferencing tool charges users per minute or hour of meeting time.

Benefits:

- Transparent pricing based on usage duration

- Encourages prolonged engagement

- Simplifies billing for continuous usage

Hybrid Metering

Combines elements of event-based and time-based metering for flexible pricing models.

Example: A SaaS analytics platform charges per report generated (event-based) and per hour of platform access (time-based).

Benefits:

- Greater flexibility in pricing

- Addresses diverse customer needs

- Enables sophisticated revenue strategies by combining multiple metrics

Integrating UBB with existing billing systems

Integrating UBB with existing billing systems requires careful planning and implementation to ensure operational continuity and data integrity. You should assess compatibility between UBB solutions and current billing platforms, considering API integrations, data synchronization, and scalability. Seamless integration enables you to streamline billing processes and provide a unified customer experience while leveraging existing infrastructure investments.

Addressing common implementation challenges

Implementing UBB can present challenges such as complexity in pricing structures, regulatory compliance, and customer communication. You must proactively address these challenges by defining clear pricing rules, ensuring compliance with data privacy regulations, and communicating pricing changes transparently to customers. Additionally, leveraging analytics and customer feedback helps refine UBB strategies over time, optimizing customer satisfaction and revenue growth.

Chapter 4: Best Practices for Effective Usage-Based Billing

Designing pricing tiers and structures

When crafting pricing tiers and structures for usage-based billing (UBB), aligning them with customer needs and usage patterns is crucial. Begin by categorizing your customer base into cohorts to grasp their diverse needs and willingness to pay. We recommend evaluating the value metrics of your product, service, and offerings. Reflect on the outcomes you facilitate and identify key metrics that signify success. Determine which metrics can be monetized and how to leverage them effectively.

This segmentation will guide the creation of tiered pricing that offers clear value propositions at each level. This will encourage customers to choose plans that best fit their usage intensity and budget. You should also consider the scalability of your pricing tiers to accommodate growth and changes in customer behavior over time.

Communicating UBB to customers

Transparent communication is essential in usage-based billing (UBB) to build trust and ensure customer satisfaction. Clearly articulate how usage is measured, what constitutes each unit of usage, and how charges are calculated. Provide accessible tools and dashboards that allow customers to monitor their usage in real-time and understand their billing statements. Use plain language and avoid jargon to improve clarity. Most importantly, proactively communicate any pricing or usage terms changes to maintain transparency and prevent surprises that can lead to churn.

Managing and optimizing pricing strategies

Effective management and optimization of pricing strategies in usage-based billing (UBB) require continuous monitoring and analysis. Leverage data analytics to gain insights into customer behavior, usage patterns, and market trends, allowing you to dynamically adjust pricing tiers and structures. This approach not only maximizes revenue but also aligns with customer demand. Incorporate a flexible product catalog that supports a variety of pricing strategies, enabling you to mix and match plans, add-ons, and one-time charges. Additionally, ensure your billing system allows for tailored pricing adjustments for specific customers or grandfathering legacy pricing, helping to minimize disruption and churn. Implement dynamic pricing mechanisms where applicable to respond to fluctuations in demand or operational costs, and regularly review your pricing strategies to maintain competitiveness and alignment with business objectives.

Balancing flexibility with predictability in billing

Achieving the right balance between flexibility and predictability in billing is essential for customer satisfaction and business stability. Offer flexible billing options that accommodate varying usage and seasonal fluctuations while maintaining clear pricing structures to ensure predictability. Provide customers the freedom to upgrade or downgrade their plans without penalty, enhancing their experience. At the same time, establish predictable billing cycles and payment terms to support financial planning for your customers and your company. Additionally, consider implementing automated entitlement management to optimize pricing and packaging by setting and adjusting feature limits, enabling agility in your operations without straining engineering resources.

> *"Chargebee empowers us to turn our business goals into actionable plans without worrying about the technical possibilities. With significant achievements in our payment collection processes, we're now exploring pricing experiments, innovative packaging, and usage-based plans to drive revenue growth."*
>
> **– JULIAN FREICHEL, TEAM LEAD –**
> **CORPORATE DEVELOPMENT, XENTRAL**

Chapter 5: UBB and Business Growth

Subscription-based businesses are constantly seeking strategies to acquire new customers and retain them over the long term. Usage-based billing (UBB) can help achieve these goals by aligning pricing with customer usage patterns and providing greater flexibility, resulting in more value for both sides.

Leveraging UBB for customer acquisition

Traditional subscription models often struggle with customer acquisition due to fixed pricing structures that may not cater to varying customer needs. UBB addresses this challenge by offering a pricing model that scales with usage and appeals to a broader audience. By allowing potential customers to pay based on their actual consumption, you can attract users who may be hesitant to commit to a flat-rate subscription. This flexibility not only lowers the barrier to entry but also enables you to tap into new markets and demographics that value pay-as-you-go options.

Increasing customer retention with personalized pricing

Customer retention is vital for the sustained growth of subscription-based companies. UBB plays a vital role by fostering deeper engagement and satisfaction among subscribers. Because revenue is directly proportional to usage, companies are incentivized to increase product usage and adoption. This again increases customer satisfaction and stickiness, resulting in better retention.

Personalized pricing based on individual usage patterns demonstrates that the service provider values their needs. It encourages customers to remain loyal as they perceive the service's value as more aligned with their personal or business requirements. Optimizing pricing based on usage data can increase customer lifetime value (CLV) and reduce churn rates effectively.

Scaling operations and infrastructure with usage-based billing

As subscription businesses grow, so do the challenges associated with scaling operations and infrastructure. UBB offers a scalable pricing framework that can accommodate fluctuations in demand and usage patterns without requiring significant adjustments to existing systems. However, choosing the right revenue growth provider is crucial to fully leverage these benefits and ensure sustainable growth in a dynamic market. This scalability extends beyond billing, influencing resource allocation, service provisioning, and operational efficiency.

Integrating usage-based billing into your subscription model isn't just about adapting to current market trends—it's about future-proofing your business. By leveraging UBB to drive customer acquisition, increase retention through personalized pricing, and scale operations efficiently, you can position yourself for sustainable growth.

Chapter 6: A UBB Success Story

How Europe-based Yousign Handled hyper-growth

Navigating the European SaaS market poses numerous challenges - diverse payment and language preferences, complex compliance regulations, and evolving security standards. From eIDAS in 2014 to GDPR in 2018 and PSD2 in 2019, the regulatory landscape is constantly changing.

Since 2013, Yousign has overcome these obstacles, establishing a stronghold in the European e-signature sector. With over 6,000 customers, this industry leader has effectively localized its operations in France, the United Kingdom, Germany, Belgium, Italy, Spain, and the Netherlands.

After four years of operations, Yousign moved to the subscription business model to maximize its predictable revenue. One of its main requirements when selecting Chargebee as its subscription billing and revenue growth platform was the ability to implement a hybrid pricing strategy. Yousign needed to offer per-user pricing for its app, based on the size of teams using the solution within an organization and tiered pricing for the API service based on the volume of signatures consumed by enterprises.

The result? With Chargebee's support for every possible pricing model, Yousign nailed its pricing strategy by implementing a per-user pricing structure in tandem with tiered pricing. That's hybrid pricing for the win!

Chargebee allows us to implement a hybrid pricing strategy: per-user pricing for our app based on seats and tiered pricing for the API service which is based on the usage volume. Chargebee allows us to grow as we make pricing changes and as we add more customers and product lines

Antoine Louiset
Co founder and CTO, Yousign

Chapter 7: Future Trends in Usage-Based Billing

The shift towards automation and AI-driven processes is reshaping traditional business models, including pricing strategies. Historically, seat-based pricing tied costs to the number of users, irrespective of actual usage. However, as AI replaces manual processes and increases efficiency, the value prop of seat-based pricing may decrease. Usage-based billing emerges as a solution that aligns costs directly with consumption, offering a fairer and more transparent pricing structure. This trend reflects a broader technological shift and response to market demands for flexibility and cost-effectiveness.

The future of pricing is hybrid

Looking ahead, industry experts agree that the future of pricing lies in hybrid models. While pure usage-based billing models have gained traction for their flexibility, they may only be suitable for some services or industries. Hybrid models, combining subscription and usage-based billing elements, offer businesses the versatility to cater to diverse customer needs. This approach allows you to balance predictable revenue streams with capturing additional revenue from usage spikes, maximizing profitability and customer satisfaction.

Emerging technologies and their impact on UBB

Emerging technologies such as artificial intelligence, blockchain, and the Internet of Things (IoT) are poised to revolutionize UBB implementations. One fundamental disruption that AI introduces is the need for companies to reevaluate the sustainability of their pricing models, even for those already utilizing UBB. Current pricing structures are often based on existing hypotheses about the outcomes delivered. However, as these outcomes evolve—such as with the introduction of new AI offerings that increase customer efficiency but could negatively impact margins if not integrated into monetization strategies—companies must critically assess their pricing structures and unit economics. This reevaluation is pivotal for adapting to rapid changes in the market and ensuring long-term viability. AI will further facilitate this process through predictive analytics and dynamic pricing adjustments based on real-time data insights.

Predictions for the future of usage-based billing

The UBB landscape will continue to evolve rapidly over the next five years. While some predict the demise of UBB in its current form, the reality is more nuanced—the future is hybrid. Businesses will increasingly adopt hybrid models that blend subscription-based and usage-based elements to meet evolving market demands. This approach accommodates varying customer preferences and supports sustainable revenue growth and scalability.

The future of UBB hinges on innovation and adaptation to emerging technologies. Subscription-based businesses can stay ahead of the curve by embracing hybrid models, leveraging AI and IoT advancements, and staying attuned to market dynamics.

Conclusion

In this ebook, we've explored the potential of usage-based billing (UBB) for subscription-based businesses. From customer acquisition and retention to scaling operations and adapting to future trends, UBB is more than just a pricing model—it's a strategic approach to future-proof revenue and fuel sustainable growth.

Learn more about usage-based billing from Chargebee and get a demo to unlock the power of subscription billing for your business.

Get a Demo:

chargebee